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Asia's astonishing rebound

Print edition August 15th 2009

Asia's astonishing rebound
Asia's emerging economies are leading the way out of recession; now they must make their recovery last: leader



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Politics this week

Aug 13th 2009
From The Economist print edition

France and **Germany** took observers, and markets, by surprise by notching up small increases in economic growth for the second quarter, and so exiting recession. GDP in the 16-country euro area declined by 0.1%, and in the wider European Union by 0.3%. The gloom got deeper in the struggling **Baltics**, however, as Estonia, Latvia and Lithuania all reported big falls in quarterly GDP. Latvia's credit rating was downgraded by Standard & Poor's. See article

Four more bombs went off in the Spanish island of Majorca, though nobody was hurt. The violent Basque separatist group **ETA**, which wants to disrupt tourism in Spain, took responsibility.

A Russian charity worker and her husband were abducted and shot dead in **Chechnya**. This was the latest of many such killings in the north Caucasus. See article

Russia's president, Dmitry Medvedev, attacked his Ukrainian counterpart, Viktor Yushchenko, for his anti-Russian stance. In a clear bid to influence next January's presidential election, Mr Medvedev said he was waiting for new leadership in Ukraine.

Election tactics

A court in Yangon sentenced Aung San Suu Kyi, leader of **Myanmar's** opposition, to a further 18 months in detention. She was found guilty of breaking the terms of her house arrest by being visited by an American who swam across the lake by her home in May. The sentence ensures that she will be incarcerated during an election the ruling junta plans to hold next year. See article

Indonesia's Constitutional Court rejected challenges by the two losing candidates to the victory of Susilo Bambang Yudhoyono in last month's presidential election. It said there was no evidence of systematic electoral fraud.

Clashes on the island of Basilan in the southern **Philippines** between the army and the Abu Sayyaf terrorist group killed at least 43 people.

AFP



At least 67 people died in **Taiwan** in floods and mudslides caused by Typhoon Morakot. Hundreds of people who had been missing were found safe days after the disaster struck. See article

Violence intensified as **Afghanistan** prepared for presidential elections on August 20th. Taliban militants carried out fierce attacks on police headquarters in both Logar and Kunduz provinces. See article

American and Pakistani officials claimed that Baitullah Mehsud, leader of the **Pakistani Taliban**, had been killed in a strike by an unmanned American aircraft. Taliban spokesmen denied he was dead, though some said he was seriously ill. See article

Reigniting terror?

AP

A spate of bombings in Baghdad and Mosul in **Iraq** left at least 100 civilians dead and hundreds more wounded. Al-Qaeda and other Sunni insurgents were blamed for the well-planned attacks. The upsurge in violence comes a month after American forces withdrew from Iraq's towns and cities, handing over security to Iraqi forces. See article

In **Iran**, the authorities admitted that 4,000 people had been detained during

the mass protests that followed the disputed June 12th presidential election. An opposition leader, Mehdi Karroubi, claimed that both female and male prisoners suffered brutal and repeated sexual torture. See article



The first party congress for 20 years held by the **Palestinians'** Fatah party ended with the election of a majority of new people to its most important executive committee. Beset by cronyism and corruption, delegates hope the new leadership will reform the party and make it more competitive with its Islamist rival, Hamas. See article

On her seven-country tour of Africa, a tetchy **Hillary Clinton** snapped at a student who asked her what Mr Clinton thought about a loan to Congo. Mrs Clinton replied, "My husband is not the secretary of state. I am," perhaps feeling a bit bruised at the praise lavished upon Bill Clinton after his mission to free two American journalists in North Korea. See article

The dog days of summer

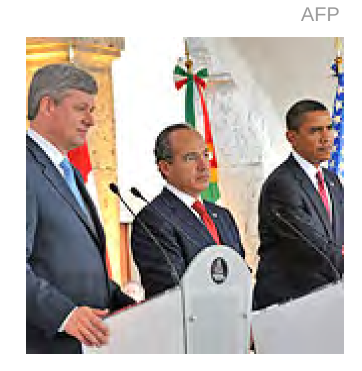
The debate in America over **health-care reform** turned rancorous. Congressmen were shouted down by opponents of Barack Obama's plans as some town-hall meetings held to discuss the plans became disruptive. Democrats claimed the protests were organised by Republican groups. See article

Mel Martinez said he would step down as a senator for **Florida** before the autumn. Mr Martinez, a Republican, had already declined to seek re-election next year. His decision to retire sooner complicates things for Charlie Crist, the governor, who is running for the seat and must now appoint someone to the vacancy.

Sonia Sotomayor was sworn in as a Supreme Court justice after the Senate voted 68-31 to confirm her nomination. Ms Sotomayor, the first Hispanic judge on the court, picked up the support of nine Republican senators.

Goods neighbours

AFP



Barack Obama expressed support for Mexico's fight against drug gangs at the annual summit of **North American leaders**. But he disappointed Stephen Harper, Canada's prime minister, and Felipe Calderón, Mexico's president, by parrying their calls to scrap "Buy American" provisions in his fiscal stimulus law.

A meeting of **South American presidents** called for Mr Obama and Colombia's Álvaro Uribe to give reassurances that an agreement under which the United States will gain increased access to Colombian military bases for surveillance of drug-traffickers would not threaten other countries. Venezuela's Hugo Chávez claimed that "winds of war" were blowing. See article

Manuel Zelaya, **Honduras's** ousted president, urged Mr Obama to do more to restore him to power. In Tegucigalpa, the capital, 55 people were arrested in clashes between police and Zelaya supporters.

Police in **Brazil** accused Wallace Souza, a television presenter and local politician in the city of Manaus, of drug-trafficking and ordering killings of rival traffickers to boost ratings. Mr Souza said the claims were smear attempts.

A prosecutor in **Peru** filed charges of murder against two police generals and 15 other officers over the crushing of protests by Amazonian Indians in which 23 police and ten civilians were killed.

Óscar Arias, **Costa Rica's** president, became the first head of state to be taken ill with swine flu.

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Business this week

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America's **Federal Reserve** decided not to increase its $300 billion programme of buying Treasury debt with newly printed money, though it did push back the completion date and left open the option of future purchases. The **Bank of England** decided recently to expand its plan to purchase assets, mostly gilts, by £50 billion ($83 billion), to £175 billion. Mervyn King, the governor of the Bank of England, hinted that, given the parlous state of the British economy, "quantitative easing" would continue. See article

Chinese officials downgraded an accusation against four employees of **Rio Tinto** from state espionage to the less serious complaint of obtaining trade secrets. The case against the Anglo-Australian mining group is complicated by contradictory signals from China's state-secrets watchdog, which backed away from an earlier claim that through "deceit", Rio had cost China $100 billion by overcharging for its iron ore. See article

Australia's **Felix Resources** pondered a takeover bid from China's **Yanzhou Coal Mining**, the latest instance of China's growing appetite for acquisitions in Australia's mining sector.

BHP Billiton, Rio Tinto's larger rival, ended a six-year run of record profits. Net income for the year to June 30th fell by 62%, to $5.9 billion.

Feeding the dragon

China notched up record imports of **oil** and **iron ore** last month, amid rising demand for exports. China imported 4.6m barrels of oil a day in July (equivalent to over half of Saudi Arabia's daily output) and 58.1m tonnes of iron ore.

America claimed an "important step" had been taken towards opening market access for **American goods in China** after the World Trade Organisation published a ruling that Beijing must lift restrictions on imports of copyrighted films, DVDs and books. The distribution of entertainment products is limited to state enterprises, which America says increases the demand for pirated goods.

Principles in the principality

Britain reached an accord with **Liechtenstein** in which the tiny country's banks will be required to ask their British clients if their tax records are in order, and given the chance to pay back taxes in return for lighter penalties. In April the G20 declared a clampdown on tax havens.

A judge postponed a decision to approve **Bank of America's** proposed deal with the **Securities and Exchange Commission**, which settles allegations that the bank misled investors about executive bonuses at Merrill Lynch. BoA took over Merrill during last September's financial maelstrom; the bonuses sparked a furore when they came to light. The judge said he had "continued misgivings" about the settlement, in which BoA neither admits nor denies wrongdoing.

American International Group posted its first quarterly net profit since the third quarter of 2007. The troubled insurer benefited from a change in the way financial companies can value troubled assets. Robert Benmosche, formerly of MetLife, started his job as AIG's new chief executive. See article

Royal Bank of Scotland lost £1 billion ($1.7 billion) after tax in the first half of the year as impairment charges on toxic loans soared. **ING**, a Dutch bank that has racked up huge losses, reported a small quarterly profit, its first for a year.

After a lengthy pursuit, **Friends Provident**, a British life insurance and pensions provider, agreed to a £1.9 billion ($3.1 billion) takeover from Clive Cowdery's **Resolution**.

Toshiba said it would start manufacturing **Blu-ray disc** players. Until last year the company had championed the rival HD DVD camp in the "format wars" against Sony's Blu-ray standard for control of the high-definition film-disc business. Blu-ray was eventually adopted by the big Hollywood studios.

A report from the OECD found that **mobile-phone charges** among its 30-member countries were highest in Canada, Spain and the United States, and lowest in Finland, the Netherlands and Sweden. Although mobile charges fell across the board on average, prices remained high in North America where users often have to pay to receive a call.

American employers shed 247,000 **jobs** in July, the lowest number since August last year. July's unemployment rate fell slightly, to 9.4%. See article

Not so sweet

The price of **sugar** rushed to 28-year highs as bad weather in Brazil and India, the biggest producers, affected crops. Food companies in the United States said they could "virtually run out" of the commodity and warned of job cuts unless the government eased restrictions on imports of tariff-free sugar. America and Europe subsidise their sugar producers.



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KAL's cartoon

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Illustration by KAL

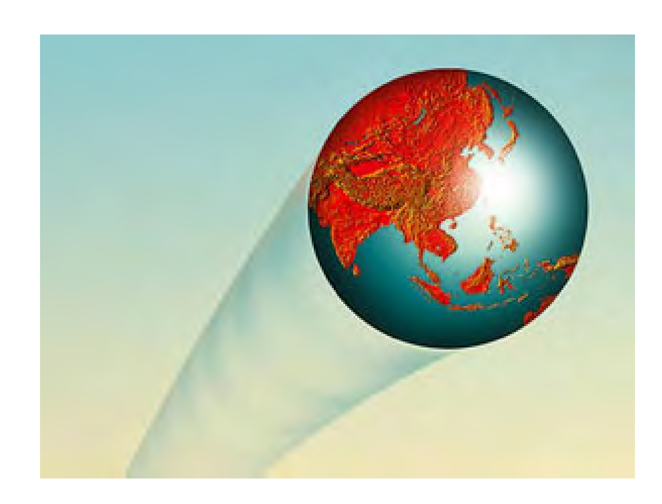


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An astonishing rebound

Aug 13th 2009
From The Economist print edition

Asia's emerging economies are leading the way out of recession; now they must make their recovery last



IT NEVER pays to underestimate the bounciness of Asia's emerging economies. After the region's financial crisis of 1997-98, and again after the dotcom bust in 2001, outsiders predicted a lengthy period on the floor—only for the tigers to spring back rapidly. Earlier this year it was argued that such export-dependent economies could not revive until customers in the rich world did. The West still looks weak, with many economies contracting in the second quarter, and even if America begins to grow in the second half of this year, consumer spending looks sickly. Yet Asian economies, increasingly decoupled from Western shopping habits, are growing fast.

The four emerging Asian economies which have reported GDP figures for the second quarter (China, Indonesia, South Korea and Singapore) grew by an average annualised rate of more than 10% (see article). Even richer and more sluggish Japan, which cannot match that figure, seems to be recovering faster than its Western peers. But emerging Asia should grow by more than 5% this year—at a time when the old G7 could contract by 3.5%. Western politicians should brace themselves for more talk of economic power drifting inexorably to the East. How has Asia made such an astonishing rebound?

Out of smoke and mirrors, say some Western sceptics. They claim China's bounceback is yet another fake. The country's numbers are certainly dodgy: the components of GDP do not add up, and the data are always published suspiciously early. China's economy probably slowed more sharply in late 2008 than the official numbers suggest. But other indicators, which are less likely to be massaged, confirm that China's economy is roaring back. Industrial production rose 11% in the year to July; electricity output, which fell sharply last year, is growing again; and car sales are 70% higher than a year ago.

And surely the whole of Asia cannot be engaged in a statistical fraud. South Korea's GDP grew by an annualised 10% in the second quarter. Taiwan's probably increased by even more: its industrial output jumped by an astonishing annualised rate of 89%. India was hit less hard by the global recession than many of its neighbours because it exports less, but its industrial production has also perked up, rising by a seasonally adjusted rate of 14% in the second quarter. Output in most of the smaller Asian economies is still lower than a year ago, because they suffered steep downturns late last year. But at economic turning points, one should track quarterly changes.

Thrift in the boom, stimulus in the slump

Asia's rebound has several causes. First, manufacturing accounts for a big part of several local economies, and industries such as cars and electronics are highly cyclical: output drops sharply in a downturn and then spurts in the upturn. Second, the region's decline in exports in late 2008 was exacerbated by the freezing up of global trade finance, which is now flowing again. Third, and most important, domestic spending has bounced back because the fiscal stimulus in the region was bigger and worked faster than in the West. India aside, the Asians entered this downturn with far healthier government finances than rich countries, allowing them to spend more money. Low private-sector debt made households and firms more likely to spend government handouts; Asian banks were also in better shape than their Western counterparts and able to lend more. Asia's prudence during the past decade did not allow it to escape the global recession, but it made the region's fiscal and monetary weapons more effective.

Western populists will no doubt once again try to blame their own sluggish performance on "unfair" Asia. Ignore them. Emerging Asia's average growth rate of almost 8% over the past two decades—three times the rate in the rich world—has brought huge benefits to the rest of the world. Its rebound now is all the more useful when growth in the West is likely to be slow. Asia cannot replace the American consumer: emerging Asia's total consumption amounts to only two-fifths of America's. But it is the growth in spending that really matters. In dollar terms, the increase in emerging Asia's consumer-spending this year will more than offset the drop in spending in America and the euro area. This shift in spending from the West to the East will help rebalance the world economy.

Beijing, Bangkok and Bangalore: beware boastfulness

It is easy to boost an economy with lots of government spending. But Asian policymakers now face two difficult problems. Their immediate dilemma is how to sustain recovery without inflating credit and asset-price bubbles. Local equity and property markets are starting to froth. But policymakers' reluctance to let their currencies rise faster against the dollar means that their monetary policy is, in effect, being set by America's Federal Reserve, and is therefore too lax for these perkier economies. The longer-term challenge is that once the impact of governments' fiscal stimulus fades, growth will slow unless economic reforms are put in place to bolster private spending—something Japan, alas, never did (see article).

Part of the solution to both problems—preventing bubbles and strengthening domestic spending—is to allow exchange rates to rise. If Asian central banks stopped piling up reserves to hold down their currencies, this would help stem domestic liquidity. Stronger currencies would also shift growth from exports to domestic demand and increase households' real spending power—and help ward off protectionists in the West.

Hubris is the big worry. With the gap in growth rates between emerging Asia and the developed world heading towards a record nine percentage points this year, Chinese leaders have taken to warning America about its lax monetary policy (while Washington has stopped lecturing China about the undervalued yuan). But it would be a big mistake if Asia's recovery led its politicians to conclude that there was no need to change their exchange-rate policies or adopt structural reforms to boost consumption. The tigers' faster-than-expected rebound from their 1997-98 financial crisis encouraged complacency and delayed necessary reforms, which left them more vulnerable to the global downturns in 2001 and now. Make sure this new rise is not followed by another fall.

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Latin America's new alliances

Whose side is Brazil on?

Aug 13th 2009
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Time for Lula to stand up for democracy rather than embrace autocrats

AP



THIS is a grand time to be a Brazilian, and especially to be Luiz Inácio Lula da Silva, the country's inspirational president. Long the chronically underperforming giant of Latin America, Brazil is now on every list of the half-dozen or so new places that matter in the 21st century. It seems that no international gathering, be it to discuss financial reform or climate change, is complete without Lula, a former metal worker and trade-union leader whose bonhomie and instinct for conciliation between political opposites make him friends everywhere. "He's my man," gushed Barack Obama at the G20 summit in London; Fidel Castro calls him "our brother Lula".

Brazil's new prominence is deserved. It stems in large part from the success of Lula and his predecessor, Fernando Henrique Cardoso, in stabilising a previously dysfunctional economy, ushering in faster economic growth. Already one of the ten biggest economies, it was one of the last of them to enter recession and now looks like being one of the first to leave it. When Goldman Sachs bracketed it with China, India and Russia as the BRIC economies and said they would dominate the world by 2050, there was much sniffing that Brazil did not belong in such muscular company. Certainly the BRIC tag has done Brazil a marketing favour. But it is now Russia, with its depressed, oil-dependent economy, that looks like the misfit.

Lula, too, deserves much of the praise heaped upon him. On taking office in 2003, he showed political courage in sticking to responsible economic policies, ignoring calls from his left-wing Workers' Party to default on debt. His instinct for rational economics has turned him from a protectionist into a champion of free trade. His ambitious social policies have helped to lift 13m Brazilians out of poverty; searing inequalities of income are narrowing steadily. Despite almost supernatural popularity ratings, he has wisely rejected talk of changing the constitution to run for a third term.

Success at home has given oxygen to the vaulting ambition of Lula's foreign policy. His Brazil wants to be seen as a great power by setting itself up as the leader of a united Latin America while also seeking new alliances with other rising powers of the global "south". Thanks to Lula's ability to be all things to all men, thus far Brazil has achieved influence without being weighed down by responsibility. But look more closely and he risks bequeathing a disappointingly ambivalent legacy. Above all, Brazil needs to decide what it stands for and who its real friends are—or risk that others make that choice for it.

Southern successes and discomforts

Though history has also given it kinship with Africa, whence millions were brought as slaves, Brazil is at first sight the most "Western" of the BRICs. Unlike China or Russia, it is a democracy in a mainly

democratic region. But Brazil's leaders have often preferred to see their country as a "southern" power, a leader of the developing world. Under Lula, this bias has hardened. In some ways this is healthy. Lula is right to call for the world's institutions to be reshaped to reflect a changing balance of power. Brazil's exports have found new markets in Asia, Africa and the Middle East. But what really unites these countries? To Brazil's chagrin, China helped block its bid for a permanent seat on the United Nations Security Council, while India did much to stop a world-trade deal. And the southern bias has gone hand-in-hand with more negative traits.

Admirably for a would-be great power, Brazil has renounced nuclear weapons. Less admirably for a country which defends the Nuclear Non-Proliferation Treaty, it has refused to sign an improved safeguards protocol, denying international inspectors full access to its civilian nuclear facilities.

Lula's government also shows a puzzling disregard for democracy and human rights beyond Brazil's borders. Celso Amorim, his foreign minister, argues that condemnations by rich countries of abuses in poor ones are biased and ineffective. Human-rights groups complain that at the UN Brazil aligns itself with countries like China and Cuba to protect abusive regimes. Lula congratulated Mahmoud Ahmadinejad on his victory in Iran's deeply flawed election, comparing massive opposition protests to those of football fans whose side has lost. Mr Ahmadinejad's first post-inauguration foreign trip will be to Brasília. Mr Obama has asked Lula to "use his influence" to persuade his guest to curb his suspect nuclear work. If Brazil takes up a rotating seat at the UN Security Council next January, it may have to choose whether to back tougher sanctions against Iran.

No triangulation between democrats and autocrats

In many of these stances there is a tacit streak of anti-Americanism. This is costliest for Brazil in Latin America. *Yanqui* influence there is in relative decline, while the sway of China and others is growing (see article). If there are now fears of a "new cold war" in the region, as some in Brazil worry, the man who threatens to start it is not Mr Obama but one of Lula's dodgiest friends, Venezuela's Hugo Chávez.

Yes, Mr Chávez is elected, but he shows ever-fewer signs of being prepared to relinquish power at the ballot box and constantly stirs up tensions in the region. It was fear that Honduras's president was turning his country into the latest *chavista* domino that prompted the misguided coup there in June. Now Mr Chávez threatens war against Colombia because it is updating an agreement under which it grants facilities at military bases to the United States, which is helping it fight FARC guerrillas and other drug traffickers. Only the paranoid can construe this as a threat to Venezuela or the Amazon. Yet Brazil chose to express concern about the bases while remaining silent about Mr Chávez's arms build-up and clear evidence that his people have sold weapons to the FARC (see article).

Nobody should expect Brazil to act as America's sheriff. But it is in its own interest to prevent a new cold war in the region. The way to do so is not to equivocate between democrats and autocrats, as Lula seems to think. It is to shame Mr Chávez by drawing a clear, public line in favour of democracy—the system that allowed a poor lathe-operator to come to power and change Brazil. Why should other countries deserve less?

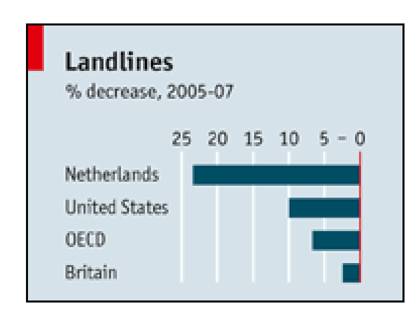
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The decline of the landline

Unwired

Aug 13th 2009
From The Economist print edition

As more people ditch landline phones for mobiles, America's regulators need to respond



IF YOU want to save money, cut the cord. In these difficult times ever more Americans are heeding this advice and dropping their telephone landlines in favour of mobile phones (see article). Despite some of the flakiest mobile-network coverage in the developed world, one in four households has now gone mobile-only. At current rates the last landline in America will be disconnected sometime in 2025.

Good. Mobile phones offer individuals more freedom. Yet confronted by the inexorable march of progress, America's telecoms regulators have failed to respond. In many ways the landline network is still an essential utility. Maintaining landline networks provides thousands of jobs (the landline operators support more pensioners than even the car industry does). Landlines are the platform for many public services, such as emergency response. And taxes on landlines are the basis of the complex system of subsidies to ensure universal service, meaning an affordable phone line for all.

The phone network is thus not just a technical infrastructure, but a socioeconomic one. The more Americans abandon it to go mobile-only or make phone calls over the internet, the more fragile it becomes: its high fixed costs have to be spread over ever fewer subscribers. If the telephone network in New York State were a stand-alone business, it would already be in bankruptcy. In recent years it has lost 40% of its landlines and revenues have dropped by more than 30%.

But copper landlines are now an obsolete technology. Telephony, once the mainstay of the industry, is just one service that can be offered over broadband connections, which will increasingly depend on new fibre-optic and wireless technology, not copper. Rather than trying to keep a 19th-century technology alive, America's telecoms rules must be updated to foster the roll-out of this new, 21st-century infrastructure. Alas, attempts to reform the notoriously bureaucratic Universal Service Fund, the main source of subsidies to make landlines affordable, have gone nowhere. Everyone agrees on the importance of expanding access to broadband—until it is time to hammer out the specific details. Now Barack Obama wants a national strategy. He would do well to concentrate on two things his country needs in the future, not the past: better and more reliable wireless coverage; and more broadband connections, through fibre-optic cables and high-speed wireless links (for both voice and data). America ranks 15th in broadband penetration among OECD countries.

Kept on hold

America's advantage is that so many people have gone before it. To extend wireless coverage to rural areas, where subsidies are inevitable, India has an elegant reverse-auction scheme, under which the supplier who asks for least cash to supply a particular area wins the contract. With broadband networks, the role of the state has less to do with limiting handouts than increasing choice. Fibre-optic networks can be run like any other public infrastructure: government, municipalities or utilities lay the cables and let private firms compete to offer services, just as public roadways are used by private logistics firms. In Stockholm, a pioneer of this system, it takes 30 minutes to change your broadband provider. Australia's new $30 billion all-fibre network will use a similar model. There are hard choices for Mr Obama's people to make—but sticking with old rules devised for copper wires is not one of them.

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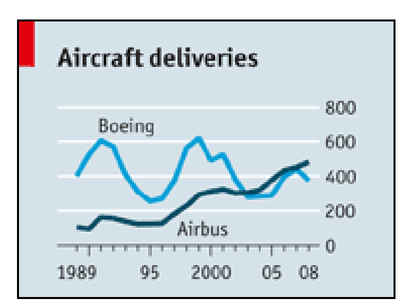


World trade and commercial aircraft

A dogfight no one can win

Aug 13th 2009
From The Economist print edition

Negotiation, not litigation, is the best way to limit the subsidies to Airbus and Boeing—and stop a trade war



AFTER five years of litigation and almost 100 bound volumes of evidence, the World Trade Organisation (WTO) is about to deliver its preliminary ruling on America's (for which read Boeing's) complaint against the provision of prohibited subsidies to Europe's commercial aircraft industry (for which read Airbus). The United States alleges that this support was worth $200 billion over 20 years. Whatever the outcome—and Boeing is confident of victory—this will be only the first stage of a lengthy process (see article). In a few months the WTO will rule on a counter-claim by the European Union that Boeing received about $24 billion in subsidies over the past two decades as well as large, non-repayable benefits from military and space contracts. Both rulings are subject to appeal. Peter Mandelson, Europe's trade commissioner before becoming Gordon Brown's minister for everything, described the dispute as the biggest, most difficult and most expensive in WTO history. This first ruling is a potential thunderbolt that could ignite a damaging trade dispute between America and Europe at a time when both economies need to present a united front on trade, to prevent a slide towards protectionism.

The origins of the dispute lie in America's decision, at Boeing's prompting, to withdraw in 2004 from a 12-year-old bilateral agreement with Europe governing trade in large civil aircraft. The agreement banned direct production and sales subsidies, but let governments continue to funnel money into new aircraft projects. It permitted both repayable direct state aid (the European approach) covering up to a third of all development costs, known as launch aid, and indirect state aid (the American approach) if limited to 3% of the domestic industry's sales volume. Boeing, however, says it expected the deal to lead to a gradual reduction in subsidies to Airbus. When this failed to materialise, it withdrew. What caused its patience to run out? Two things: the success of Airbus in achieving rough market-share parity at the end of the 1990s, and resentment over launch aid for the A380, the superjumbo designed to bring to an end the long reign of the 747. Boeing also wanted to shield its 777 and new 787 from "unfair" competition in the form of Airbus's launch-aid-supported A350.

A target-rich environment

Boeing is right to argue that all subsidies distort competition. But although the subsidies that Airbus receives are different from Boeing's, they are not necessarily much worse. At least they are transparent—and Europe claims that by 2007 Airbus had repaid 40% more than it had been given. Nor has the effect of the subsidies received by both firms been anti-competitive. Boeing and Airbus fight like rats in a sack for every sale, with the consequence that airlines have been able to buy cheaper and better aircraft than if one firm had been dominant.

Two other points should be borne in mind. The first is that it is out of date to see either firm as a national champion. The size and riskiness of large commercial-aircraft projects has forced even Boeing to create extended international supply chains. Second, the aircraft-makers' subsidies pale by comparison with those doled out by governments on both sides of the Atlantic in the past year. Leaving aside the trillions of dollars spent on preventing financial collapse, industrial subsidies of a kind almost certainly illegal under WTO rules have mushroomed. General Motors alone has been propped up to the tune of $55 billion. If America and Europe were to go to war over subsidies now they would find what military planners call a "target-rich environment".

Both sides should therefore hold their fire until the WTO rules on Europe's complaint. Then, putting further litigation to one side, they should head for the negotiating table. The aim should be to secure a new deal along the lines of the old agreement, but this time with an explicit goal of phasing out the most egregious

subsidies within a reasonable period. The alternative of an escalating tit-for-tat trade dispute between Europe and America does not bear thinking about.

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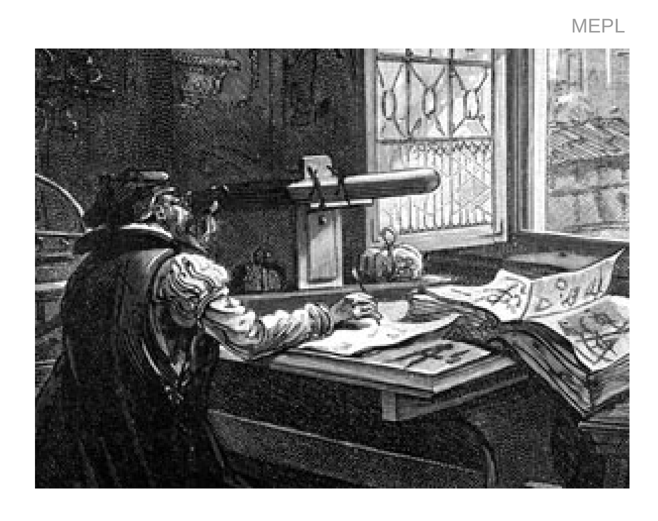
Galileo, four centuries on

As important as Darwin

Aug 13th 2009
From The Economist print edition

In praise of astronomy, the most revolutionary of sciences

MEPL



FOUR hundred years ago our understanding of the universe changed for ever. On August 25th 1609 an Italian mathematician called Galileo Galilei demonstrated his newly constructed telescope to the merchants of Venice. Shortly afterwards he turned it on the skies. He saw mountains casting shadows on the moon and realised this body was a world, like the Earth, endowed with complicated terrain. He saw the moons of Jupiter—objects that circled another heavenly body in direct disobedience of the church's teaching. He saw the moonlike phases of Venus, indicating that this planet circled the sun, not the Earth, in even greater disobedience of the priests. He saw sunspots, demonstrating that the sun itself was not the perfect orb demanded by the Greek cosmology that had been adopted by the church. But he also saw something else, a thing that is often now forgotten. He saw that the Milky Way, that cloudy streak across the sky, is made of stars.

That observation was the first hint that, not only is the Earth not the centre of things, but those things are vastly, almost incomprehensibly, bigger than people up until that date had dreamed. And they have been getting bigger, and also older, ever since. Astronomers' latest estimates put the age of the universe at about 13.7 billion years. That is three times as long as the Earth has existed and about 100,000 times the lifespan of modern humanity as a species. The true size of the universe is still unknown. Its age, and the finite speed of light, means no astronomer can look beyond a distance of 13.7 billion light-years. But it is probably bigger than that.

Nor does reality necessarily end with this universe. Physics, astronomy's dutiful daughter, suggests that the object that people call the universe, vast though it is, may be just one of an indefinite number of similar structures, governed by slightly different rules from each other, that inhabit what is referred to, for want of a better term, as the multiverse.

Star trek

The shattering of the crystal spheres which Galileo's contemporaries thought held the planets and the stars, with the sphere containing the stars representing the edge of the universe, is (along with Darwin's discovery of evolution by natural selection) the biggest revolution in self-knowledge that mankind has undergone. The world that Galileo was born into was of comprehensible compass. The Greeks had a fair idea of the size of the Earth and the distance to the moon, and so did the medievals who read their work. But these were distances that the imagination might, at a stretch, embrace. And it was easier to believe that a human-sized universe was one that might have been brought into being with humanity in mind. It is harder, though, to argue that the modern version of cosmology, let alone any hypothetical one which is

multiversal rather than universal, has come about for mankind's convenience.

Four centuries on, it is difficult to think of Galileo's intellectual heirs, meeting this week in Rio de Janeiro under the auspices of the International Astronomical Union (see article), as firebrand revolutionaries. Yet their discoveries—from planets around other stars that may support alien life, to dark matter and energy of unknown nature that are the dominant stuff of reality—are no less world-changing than his. Moderns may be more comfortable than medievals with the idea that man's notion of his place within the universe can suddenly change. That should not blind them to the wonder of it.

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Correction: America's sex laws

Aug 13th 2009
From The Economist print edition

Our leader on America's sex laws (August 8th) contained a conversion of 1,000 feet to 900 metres. It should, of course, have been approximately 300 metres. We are clearly losing touch with our Imperial past. This error has been corrected online.

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Economist.com OPINION LETTERS

On torture, hate radio, Arabic, free trade, education, the rich, Britain's monarchy, toilets

Aug 13th 2009
From The Economist print edition

Barack Obama and torture

SIR – Your briefing about the debate on torture perpetuated an unfortunate myth: that Barack Obama has dramatically altered the detention policies of his predecessor ("The dark pursuit of the truth", August 1st). The regrettable fact is that the policies implemented by Mr Obama are materially indistinguishable from those of George Bush at the end of his second term. Moreover, the Obama administration has adopted no measure that runs counter to the desires of the agencies ostensibly being regulated, including the CIA.

Support for the myth rests principally on three decisions: to close the CIA's secret "black sites", to end the use of "enhanced interrogation techniques", and to shut Guantánamo. As for the black sites, these were already empty and the CIA had long wanted to get out of the detention business. Nothing in the decision, therefore, reforms practice. In fact, Mr Obama has continued to allow the CIA to hold prisoners "temporarily" and conduct extraordinary renditions—transferring prisoners to third countries for interrogation.

With respect to American interrogation practices, the Bush administration had already ended the most loathsome abuses, including waterboarding, and the so-called "high-value" detainees, who had been subjected to these methods, were no longer being interrogated at the end of Mr Bush's second term. What's more, Mr Obama has directed American interrogators to follow guidelines in the Army Field Manual. This was drafted by the Bush administration.

Finally, there is the much-heralded decision to close Guantánamo. Granting the symbolic significance of the prison, reasonable minds would agree that what matters most is not where a prisoner is held but how. And in that regard, Mr Obama's decision to close Guantánamo is qualified in two respects. First, he has endorsed preventive detention, a wretched and morally bankrupt practice familiar to most British (and Irish) readers. Second, he has continued with the Bush-era approach that prisoners at Bagram air base in Afghanistan may be held without judicial review and he defends this with many of the same arguments that Mr Bush made about Guantánamo.

In the life of a nation, symbolic change is not meaningless. In fact, in the modern political climate, it may be all one can reasonably expect. But it should never be confused with genuine reform.

Joseph Margulies
Northwestern University School of Law
Chicago

Defending the airwaves

SIR – It is true that instances of hate media are increasing, especially in fragile states ("Crackles of hatred", July 25th). But research by our charity, an independent body created by the BBC, suggests that the use of radio during Kenya's post-election crisis was rather different from the carefully orchestrated propaganda observed during the Rwanda genocide, or in Pakistan's Swat Valley.

In the Kenyan case, supply met demand. There was pent-up anger among people who felt economically and politically marginalised and this found an outlet in newly created local-language radio. In these circumstances, simply clamping down on new media could amount to putting the lid on a pressure cooker.

James Deane
BBC World Service Trust
London

SIR – You mentioned the slaughter directed by radio of half a million people in Rwanda. Perhaps the exact techniques used to commit genocide, such as (to take Rwanda's case) radio broadcasts coupled with the use of crude *panga*-knives, are not the most important question. Nor should we restrict ourselves to studying the state apparatus needed to sustain acts of mass murder, such as the Holocaust.

The deepest conundrum is what makes groups of people, defined by religion, class, race or any other attribute, so vulnerable to political manipulation that they can be easily persuaded to commit diabolical acts against other groups. Until we solve that core problem, would-be manipulators will always find one medium or another, from the printed word to the latest form of e-communication, to demonise and proscribe the hated "other".

Dennis Sandole
Institute of Conflict Analysis and Resolution
George Mason University
Arlington, Virginia

Understanding Arabic

SIR – I enjoyed reading your long-overdue special report on the Arab world (July 25th). My one objection is your insinuation that spoken Arabic is incomprehensible between different countries. Standard Arabic is taught in all 22 Arab countries and is the official language of them all. I, for one, come from the extreme eastern corner of the Arab world, but I can communicate freely with anyone (who has been to school) in Tangier, at the extreme western corner. Mutually incomprehensible dialects are indeed common, but this is normal considering the huge distances involved. Where else do you have border crossings for 22 countries at which you are asked "Do you have anything to declare?" in the same language?

Muthana Kubba
Cham, Switzerland

* SIR – Your recognition that the "ultra-conservative Saudi royals may well be more liberal than the ultra-conservative Saudi people", misses the point. The Saudi establishment is educated in Western universities; the prime moral guide for many Saudi people is the local Wahhabi preacher. This is an all too familiar historical picture of an "enlightened" elite governing the "backward" masses who are prone to violence and disorder.

Perhaps if those liberal Saudi royals agreed to hold fully fledged municipal elections, permitted open debate in the media, stopped chopping off peoples heads and hands for wrongdoing, and allowed women to drive, to vote and get elected, then maybe Saudi public opinion would become more liberal.

Saidolimhon Gaziyev
Tashkent, Uzbekistan

Fundamentals

SIR – I was surprised that a newspaper founded in 1843 to promote free trade seemed to accept the idea, in an article on the "rising vogue" for shopping in small locally owned stores, that "local protectionism" might be a good thing for communities and for the environment ("Keeping it local", August 1st). Protectionism, at the local level or on a national scale, might temporarily benefit the protected industries, but it will eventually hinder everyone, especially the poorest.

And as for the assumption that buying goods from local suppliers benefits the environment, a study by Pierre Desrochers, a geography professor at the University of Toronto, concluded that localism and "food miles" are at best pure "marketing fads".

Quentin Michon
Paris

Education standards

SIR – I read your article on the quality of teaching in Britain and noted that "trainee teachers can resit basic literacy and numeracy tests as often as they like" ("Those who can", August 1st). At least they have to pass the tests eventually. In the United States, we have weaker requirements for aspiring teachers, and the result is apparent. A friend of mine spent several years sending back every teacher's note that her children took home, with spelling mistakes and grammatical errors corrected.

For decades teachers have been "facilitating" rather than teaching. Children are encouraged to "explore", rather than to learn; it is no longer compulsory to memorise multiplication tables, for example. Future generations will have to either clean up this mess or resign themselves to living in a country with a skill set restricted to serving up hamburgers.

Virginia Benton Morris
Carol Stream, Illinois

Rich man, poor man

* SIR – I must confess some measure of disappointment in your placid acceptance of Barack Obama's definition of "the rich" ("What now for Obamacare?", August 1st). Mr Obama has famously promised that no one with an annual income of less than $250,000 will see their taxes rise under his administration. The clear implication is that anyone earning a quarter of a million is "rich." Pardon the pun, but that's rich.

My wife and I pull in very nearly the $250,000 mark between us. However, what with student loans, a mortgage, credit-card debt from our college and law-school days, and the pesky expenses of simply living, we often find ourselves limping across the line to the next pay cheque. Our combined savings would not last us a month were we to lose our jobs, and our net worth is less than worthless.

I recognise that under the current proposals, we would supposedly not see our taxes increase (no matter how fanciful that supposition may be, according to the Congressional Budget Office). My point is that income is not a remotely plausible measure of "richness".

To be "rich", one must have wealth, not merely be a conduit for the flow of cash from employer to creditor.

Michael Slocum
Aberdeen, New Jersey

Paying for Britain's monarchy

* SIR – It is regrettable to see *The Economist* leaving unchallenged the claim that the assets of the Crown Estate belong to the Windsor family and that its income is surrendered to the state ("Buck's fizz for the masses", August 1st). The Estate was the property of the monarch before the end of the 18th century, when the king or queen had some responsibility for meeting government expenses. But this changed once the state and the person of the monarch became separate.

As a senior civil servant and before he became rector of Lincoln College, Burke Trend wrote, in an internal Treasury memo, that "the hereditary revenues which it is now customary for the Crown to surrender at the outset of each reign are simply a historical relic from much earlier days".

Joanne Horton of the London School of Economics, an expert on accountancy, has been blunter, describing the "surrender" of the Estate's revenue as "a public-relations stunt". The truth is that British taxpayers bear the entire cost of the monarchy.

John Pratt
London

* SIR – You cited Robert Walpole's famous remark to Queen Caroline that fencing in Hyde Park would cost "three crowns". However, you incorrectly said the crowns were those of England, Scotland and Ireland. The third one should be France, which was still claimed (entirely legally, in fact) by the English.

Timon Screech

Professor of the history of art
School of Oriental and African Studies
London

The Bugatti of bogs

SIR – You referred to the excellent toilets being produced in Japan as the “Lamborghini of lavatories” and the “Cadillac of commodes” (Face value, July 25th). In the spirit of alliteration, might I also suggest the “Jaguar of johns” and the “Lexus of loos”?

Sanjiv Mehta
Montreal

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* Letter appears online only

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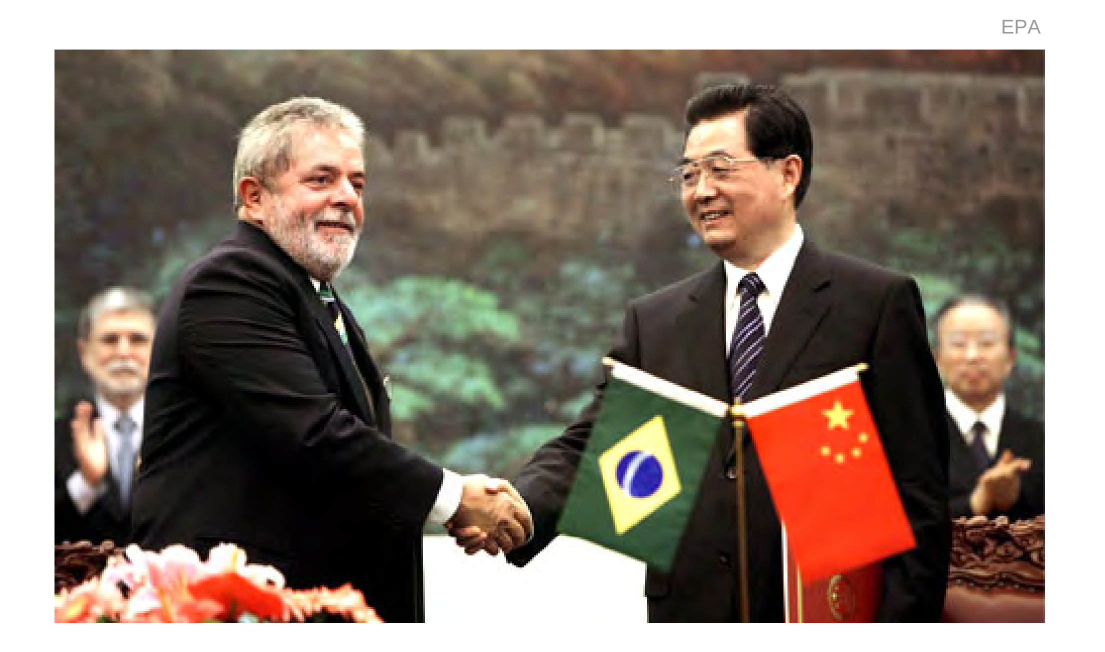
Latin American geopolitics

The dragon in the backyard

Aug 13th 2009
From The Economist print edition

Latin America is tilting towards China, Iran and the global "south"—and away from the United States

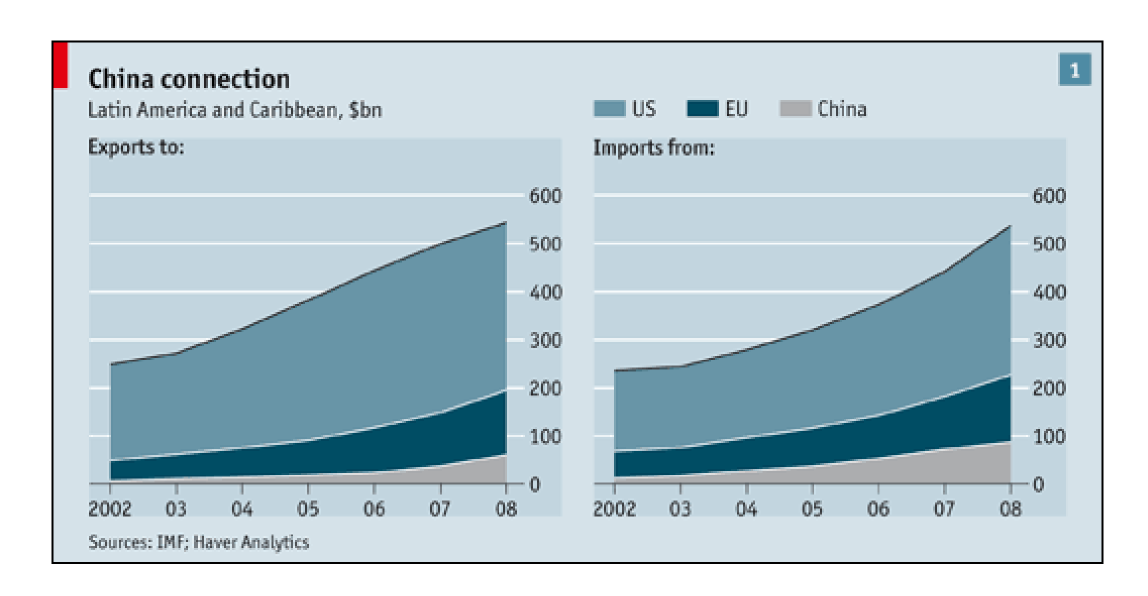
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IF ALL goes to plan, by 2012 the first shipments of copper from Toromocho, a mine in the Peruvian Andes, will be sent by train and truck to a new $70m wharf in the port of Callao. From there, they will be shipped across the Pacific to China. The mine is being developed at a cost of $2.2 billion by Chinalco, a Chinese metals giant. Both it and the wharf will be the most visible symbols of the burgeoning trade and investment that are fast turning China into a leading economic partner for Peru and many other Latin American countries.

In the first six months of this year China became Brazil's biggest single export market for the first time (partly because Brazil's manufacturing exports fell sharply in the recession). During two days of talks in Beijing in May between Brazil's president, Luiz Inácio Lula da Silva, and his Chinese counterpart, Hu Jintao (pictured above), an agreement was signed under which the China Development Bank and Sinopec, a Chinese oil company, will lend Brazil's state-controlled oil company, Petrobras, $10 billion in return for up to 200,000 barrels a day (b/d) of crude oil for ten years from the country's new deep-sea fields. Weeks earlier China offered Argentina a currency-swap arrangement involving use of yuan worth $10 billion, and lent cash-strapped Jamaica $138m to enable it to stave off a debt default. Chinese companies have bought stakes in oilfields in Ecuador and Venezuela, and are talking of building a refinery in Costa Rica. This week China National Petroleum Corporation and CNOOC, another oil firm, were reported to have bid at least $17 billion for the 84% stake in YPF, Argentina's biggest oil company, held by Spain's Repsol.

It is not just China that is taking a much bigger interest in Latin America. So too, in different ways, are India, Russia and Iran. These developments are prompting some to declare the end of the Monroe Doctrine—America's traditional insistence, voiced by President James Monroe in 1823, that any meddling by outsiders in its hemisphere is "dangerous to our peace and safety". Never mind that *Yanqui* dominance has always been disputed by Latin American nationalists as well as by Europe, and never mind that the United States (and Europe) are still far bigger traders and investors in Latin America as a whole than China, let alone India or Russia (see chart 1). What is clear is that there are new and potentially powerful actors in the region.



Their arrival coincides with, and is partly a consequence of, two other developments. The first is the relative decline in the economic and political pre-eminence of the United States after its brief moment of unchallenged power at the end of the cold war. "The centres of power are shifting and the 21st century is about the Pacific," says José Antonio García Belaunde, Peru's foreign minister. More specifically, under George Bush the United States was widely held to have neglected Latin America because of more pressing priorities elsewhere, especially the "war on terror". That neglect has helped others to slip in.

The second factor is that many Latin American countries have become more self-confident and bent on asserting their diplomatic independence. That is either because they have achieved economic stability and more robust democracies, or because they have elected left-wing governments which, for ideological reasons, are seeking new allies. Both factors apply to Brazil, which under President Luiz Inácio Lula da Silva has sought a more powerful role as a regional power of global significance (see article).

The diversification of Latin America's economic ties has raised in some minds a nagging question: does it foreshadow geopolitical changes? In the United States some Republicans worry that China's growing economic weight poses a political threat. Hillary Clinton, the secretary of state, has noted that China and Iran are making "disturbing" gains in the region. But many Latin Americans prefer to see China's expanding ties to their region as an opportunity. The region, with Brazil in the lead, is forging "south-south" alliances with China, India, Russia and South Africa to push for changes in what they all see as an unjust world economic order.

But for Latin America two other questions may be just as important, if not more so. The first is whether the industrialisation of China and India is helping or hindering its own economic development. The second is whether growing economic and political ties with non-democratic countries such as China, Russia and Iran could undermine Latin America's own hard-won commitment to democracy.

From galleons to satellites

Economic ties between Latin America and Asia are not new. From the 1560s until 1815, a fleet of Spanish galleons made an annual epic voyage from the Mexican port of Acapulco to Manila in the Philippines, carrying silver and supplies and returning with Chinese silks and porcelain that were snapped up by the wealthy in colonial Mexico and Peru. In the 1970s Japan emerged as an important trader, investor and aid donor. But the suddenness and scale of the link with China (and to a much lesser extent India) are new.

The first, and still the biggest, impact is indirect. Chinese and Indian demand for raw materials has driven world prices for commodities (of which South American countries are big producers) to unprecedented levels. This played an important role in accelerating the region's rate of economic growth to an average of 5.5% from mid-2003 to mid-2008. Second, China's trade with Latin America has grown at an annual average rate of some 40% since 2003—faster than its overall trade. China has now become a significant market for countries such as Brazil, Chile and Peru.

The rise of China prompted much gloom in Latin America a decade ago. Since average wages in China are a fifth to two-fifths of those in Latin America, it was thought that much of the region's labour-intensive manufacturing industry would be wiped out. That is why Latin American countries have tabled more anti-dumping actions against China at the WTO than has the United States.

A decade on, some of those fears have been justified, but the picture is more positive. Researchers at the World Bank have found clear net gains for the region from the expansion of China. That is largely because of the commodity effect, but also because Latin American exporters have benefited from other countries growing richer by trading with China. The bank also found no evidence that foreign direct investment was being displaced from Latin America to China. Although Latin America has a trade deficit with China, its imports are increasingly of cheap machinery, which helps it to compete in other markets.

The pain has been focused in particular countries and specific industries. Although commodity exporters such as Chile, Peru and Brazil have clearly gained, Mexico and Central American countries have fared less well. For Mexico, one of the region's most industrialised countries, China is a competitor, especially in the American market, in industries ranging from textiles to electronics. Between 2000 and 2005, China's share of American clothing imports doubled, to 26%, while Mexico's fell from 14% to 8%. But some Mexican textile producers have fought back, either by exploiting their greater closeness to the American market or by improving their quality.

Nearly all Brazil's shoemaking and toymaking has been wiped out, or has moved to China. "It's impossible to compete against China in these sectors," says Roberto Giannetti da Fonseca of São Paulo's Federation of Industries. He cites Brazil's high labour taxes and interest rates as self-inflicted handicaps. Nevertheless, South America's new links to China have helped it to ride out the world recession relatively unscathed. Marcelo Carvalho of Morgan Stanley, an investment bank, points out that Chinese demand for commodities seems to have contributed significantly to faster economic growth, a stronger currency, and lower inflation and interest rates in Brazil.

While trade has boomed, Chinese investment in Latin America has hitherto amounted to less than meets the eye. That is in contrast to India, whose trade with the region remains modest, but whose companies have begun to make significant investments in software, pharmaceuticals, business software and natural resources. It did not help that in 2004 China's Mr Hu, on the first of two visits to the region, was misquoted as announcing planned investments totalling $100 billion over ten years. (In fact, he said he hoped two-way trade would reach that figure by 2010, and that foreign investment would double, both of which are likely.)

Pumping Venezuela's oil

Chinese investment has so far been overwhelmingly concentrated in mining and oil. (An early and still unusual exception is a joint venture with Brazil, dating from the 1980s, to produce communications satellites, in which China provides 70% of the finance and the technology.) Toromocho is just one of three big investments in copper projects in Peru. Chinese companies have become the biggest foreign investors in Ecuador's oil industry.

But it is China's stake in Hugo Chávez's Venezuela that is potentially most contentious. The China Development Bank has lent two-thirds of the capital for a $12 billion joint fund which Chinese companies could tap for investment projects in Venezuela. Most of these are likely to be in oil: CNPC, a Chinese company, is operating several smallish oilfields and is investing in the Orinoco tar sands.

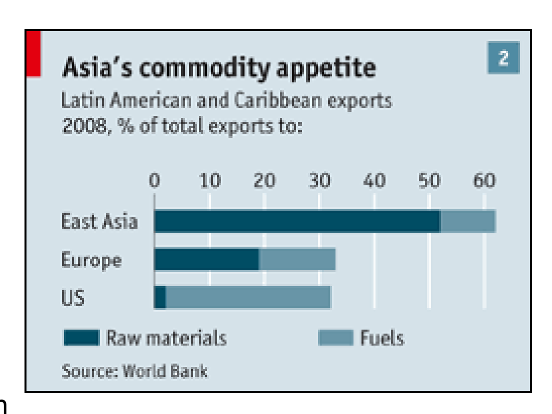
The United States has long been the main foreign market for Venezuelan oil. Venezuela provides about 10% of American oil imports, and Petróleos de Venezuela (PDVSA), the state oil monopoly, owns Citgo, an American oil distributor which has several refineries specially adapted to process the country's heavy and sulphurous crude. This mutual dependence has long been a discomfort to Mr Chávez, and he has repeatedly said that he wants to divert Venezuelan oil to China (though transport costs would be much higher). So far Venezuelan oil exports to China have risen from a negligible level to 398,000 b/d. But PDVSA has announced that it wants to increase the flow to 500,000 b/d by December. That could be done only by reducing shipments to the United States.

In Africa, China's much larger investments in oil and mining have brought accusations from some quarters that it has created neo-colonial enclaves. But in Latin America, a more developed region, China is just one of many foreign investors. After a shaky start, Chinese companies seem to have become more sensitive to local concerns. Take Peru. The first Chinese investment was by Shougang, which bought an iron-ore mine in 1992. It brought in 350 Chinese staff, and acquired a bad reputation because of constant troubles with the Peruvian workforce. In contrast, points out Luis Chang, a former Peruvian ambassador in Beijing and a consultant to Chinese firms, Toromocho has just three Chinese managers and the CEO is a Canadian.

Mr Chang is one of some 3m Peruvians who claim Chinese descent, the largest such community in Latin America. (Around 100,000 Chinese coolies were brought to Peru as labourers between 1849 and 1875,

and integrated well.) Peru has become only the second Latin American country after Chile to sign a free-trade agreement with China. Mr García Belaunde hopes this will encourage further Chinese investment, especially in sorely needed transport infrastructure, such as at Callao and other ports.

But the pattern of trade and investment so far reinforces the fear among some Latin Americans that China is causing the region to respecialise in commodities, as it did in the 19th century, to the detriment of industry. While China's exports to the region span a wide range of manufactured goods, its imports are highly concentrated in a few commodities (see chart 2). Soyabeans and iron ore account for two-thirds of Brazil's exports to China, and crude oil for a further 10%. (By contrast, Brazil's exports to the United States are mainly manufactures.) This specialisation is not necessarily damaging in itself. But as many branches of Chinese manufacturing overtake their Latin American counterparts, Latin American governments may start to place more stress on improving the competitiveness of the region's firms, partly through industrial policy.



Business and politics

Chinese officials insist that their closer relations with Latin America are driven by two things: a shared diplomatic interest in a multipolar world, and mutually beneficial economic and business ties. "We're not seeking special influence. We have reiterated [to the United States] that our relations with Latin America aren't a threat to anyone," says Qiu Xiaoqi, China's ambassador in Brasília. It is also of interest to China that half of the 24 mainly small countries around the world that still recognise Taiwan rather than China are in Latin America and the Caribbean.

Despite a flurry of presidential and ministerial visits in both directions, and mounting mutual curiosity, China and Latin America are hardly close. There are no direct flights between the two. Few Chinese are knowledgeable about the region (Mr Qiu speaks no Portuguese, though he is one of the relatively few Chinese diplomats who speak Spanish). But sooner or later China's economic involvement in Latin America seems certain to have geopolitical ramifications, requiring it to make choices. That is because of political developments within Latin America, and in particular the rise of more or less anti-American governments in some countries.

Venezuela under Mr Chávez has sought closer ties not just with China but also with Russia and Iran. During the cold war the Soviet Union bankrolled Cuba for almost three decades, and supported left-wing movements and governments throughout the region. Last year Dmitry Medvedev became the first Russian president since those days to visit Latin America. Russia also sent a small naval flotilla to the Caribbean for joint exercises with Venezuela and Cuba. This was a tit-for-tat gesture after the United States sent ships to support Georgia after its brief war with Russia last summer.

Russia's abiding interest in Latin America is focused on arms sales. Between 2005 and 2008 Mr Chávez bought Russian weapons worth $4.4 billion, including 24 Sukhoi fighters. As the oil price sank last year, shrinking Mr Chávez's kitty, Russia offered a $1 billion credit line for further arms purchases. This month Mr Chávez said he would seek "battalions of tanks" from Russia on his next visit to Moscow, in response to an agreement letting America use military bases in neighbouring Colombia. But his most worrying purchase was of 100,000 Kalashnikov automatic rifles and a production line to build more. Colombian officials fear that some of these rifles will end up with the FARC guerrillas.

EPA

Mr Chávez has also gone out of his way to court his Iranian counterpart, Mahmoud Ahmadinejad. In 2007, in Tehran, he joined the Iranians in declaring an "axis of unity" against the United States. There has been talk of nuclear co-operation. Venezuela and Cuba, along with Syria, were the only countries to support Iran's nuclear programme in a vote in 2006 within the United Nations' International Atomic Energy Agency. Mr Ahmadinejad has made two visits to Latin America, taking in Nicaragua, Ecuador and Bolivia, as well as Venezuela on both occasions. His government has opened embassies in Chile, Colombia, Ecuador, Nicaragua and Uruguay. Under an investment programme sponsored by the two governments, Iranian firms are making tractors and cars in Venezuela, and building housing for the poor.

Iran this month offered Bolivia a loan of $280m, in addition to spending $200m on building two cement factories and three milk facilities. Mr Ahmadinejad also promised Nicaragua $1 billion in aid, and Iran has announced plans to invest in Ecuador’s oil industry. But as with many of Mr Chávez’s announced investments, little cash seems to have been disbursed.



Chávez and Ahmadinejad, bosom pals

Iran’s cultivation of radical Latin American governments appears aimed partly at securing diplomatic allies in international bodies, while irritating the United States. Some analysts see a more sinister dimension, pointing to the presence in Venezuela of sympathisers with Hizbullah, the Lebanon-based Shia militia. An Argentine judge, with government backing, has issued arrest warrants for seven Iranian officials and a member of Hizbullah in connection with the bombing of the Israeli embassy in Buenos Aires in 1992 and of a Jewish community centre two years later that killed a total of 114 people and injured more than 500. But there is no firm evidence of a continuing and active Iranian-inspired terrorist presence in the region.

For China, the international entanglements of Mr Chávez and his friends are a complication rather than an attraction. “China is not very interested in radicalisms,” says Pan Wei, a political scientist at Peking University’s School of International Studies who recently spent a sabbatical term at Lima’s Catholic University; “China is not going to stir up political troubles in this area, nor have a military presence.” He points out that China forged warm relations with Chile during the dictatorship of General Augusto Pinochet.

China makes much of its pragmatic, non-judgmental approach to foreign affairs. But that might just set it on a collision course, in which it has to choose between its strategically vital relationship with the United States and Venezuelan oil. Expect it to do everything possible to avoid being faced with such a choice.

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Clean energy in the Midwest

Greening the rustbelt

Aug 13th 2009 | TOLEDO, OHIO
From The Economist print edition

In the shadow of the climate bill, the industrial Midwest begins to get ready

Xunlight



XUNLIGHT CORPORATION, a small manufacturer of solar panels, sits on a quiet street in Toledo. It has a professor as its president, about 100 employees on its payroll—and a lot of bigwig visitors. In October 2008 Sarah Palin, then the Republican vice-presidential candidate, used Xunlight as the setting for a speech on energy policy. Other guests have included Ohio's governor, two senators and a congresswoman. And no wonder: the firm provided evidence to support a seductive hope, that the green economy can help to revive the suffering rustbelt.

As the battle over a cap-and-trade bill continues in Congress, the industrial Midwest finds itself playing an awkward role. The climate bill offers two big opportunities, to reduce global warming and boost the green economy in the process. And nowhere are green jobs more loudly promoted than in the rustbelt. On August 5th Barack Obama and Joe Biden, his vice-president, travelled to Indiana and Michigan, two ailing swing states, to announce new grants to develop electric cars. But hopes for those new green jobs are matched by fears that traditional ones will be lost. With the Senate due to debate a cap-and-trade bill next month, the rustbelt and its politicians are at the heart of the battle.

The industrial Midwest has long been in need of a renaissance. Its factories have been losing jobs for decades, since long before the recession hit. Michigan, home to America's biggest carmakers, had a 15.2% unemployment rate in June, compared with a national average of 9.5%.

Green investment presents new hope. The University of Massachusetts, Amherst, and the Centre for American Progress, a think-tank, estimated in June that the federal stimulus package and a climate bill would spur about $150 billion in spending on clean energy each year for the next decade. That spending, in turn, would create an estimated 2.5m jobs, from academic researchers to factory workers making wind turbines. "This is an opportunity for American ingenuity to renew the manufacturing base," argues Phyllis Cuttino of the Environment Group at the Pew Charitable Trusts.

There are already signs of activity. The Great Lakes Wind Network, based in Ohio, helps local firms sell goods to the wind business. Toledo remains one of the best examples of a town moving from the old economy to a newer one. It has been a hub for the glass manufacturing since the 19th century. Thanks to innovations in solar technology at the University of Toledo, it is now home to a cluster of firms such as Xunlight. State grants continue to help the university hatch companies. The Regional Growth Partnership, a local business group, provides venture capital.

In Michigan despair has bred particularly bold action. In the past five years Jennifer Granholm, the

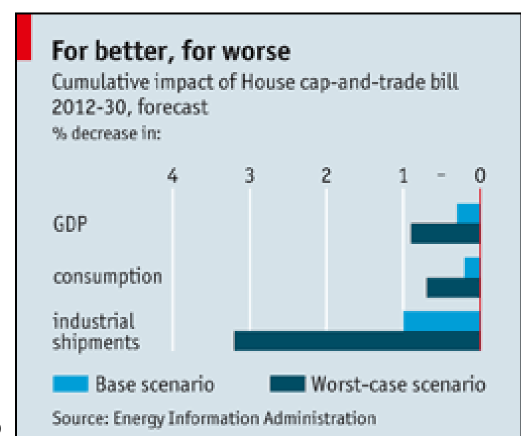
Democratic governor, has dangled more than $1 billion to attract alternative-energy firms, with about $700m in tax credits to develop electric-car batteries. Impressively, Michigan had the third-highest number of clean-tech patents from 1999 to 2008, behind only California and New York, reckons Pew. That number may rise. Last year Michigan passed a requirement for power companies to boost efficiency, along with an order that renewable sources account for 10% of the state's electricity by 2015. Investments from the federal stimulus will help too. In the share-out on August 5th, Michigan won more grants for electric cars than any other state.

Nevertheless, the clean-energy economy remains small. Though green jobs are increasing in number, they accounted for only 0.6% of jobs in Ohio in 2007, according to Pew. The shares in Michigan and Indiana were even smaller, at 0.4% and 0.5% respectively. Manufacturing, for all its troubles, is a behemoth in comparison, accounting for 14% of employment in Ohio, 15% in Michigan and 18% in Indiana in 2007. And it is a dirty giant, dependent on cheap coal. The Midwest emits an outsize share of carbon, according to a report from the Chicago Council on Global Affairs. Indiana is one of the worst offenders, spewing out 4% of America's carbon emissions in 2007 though it is home to only 2% of its population.

The fear is that a cap-and-trade bill may expand a promising new sector but devastate a struggling, larger one. Mitch Daniels, the Republican governor of Indiana, has worked hard to maintain his state's manufacturing base. A price on carbon, he argues, would threaten it.

The version of cap-and-trade passed in June by the House was meant to appease such critics. It includes help for manufacturers eager to retool for new industries. Allowances would be given away, not auctioned. And at the urging of a congressman from Michigan, the bill would, from 2020, tax imports from countries that do not restrict emissions. But some Democrats are still wary. Three of Indiana's five House Democrats voted against the bill.

Now a tough battle looms in the Senate. A new report from the Energy Information Administration (EIA) forecasts that the House bill would depress industrial shipments by 1% between 2012 and 2030 (see chart). But that assumes a quick expansion of nuclear plants, which is unlikely. In the EIA's worst-case scenario, shipments would drop 3.2%. "They're huxtering," huffs George Voinovich, Ohio's Republican senator, of the green enthusiasts. He wants more support for nuclear power and fears the House bill will transfer wealth from the heartland. On August 6th ten of Mr Voinovich's Democratic colleagues, including six from the Midwest, wrote to Mr Obama fretting that a bill would cripple manufacturing industry.



But in Toledo Xunlight's president, Xunming Deng, looks forward to a cap-and-trade bill. "Of course there is a cost, but this is an investment for our economy, for our future," he says. There remains a danger, however, that compromise will produce a clunker of a bill—one that does little to slow climate change, little to revive the old economy and little to boost a new one. Much now depends on a handful of the states in the heartland.

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The economics of natural gas

Drowning in it

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What bigger estimates of America's reserves could mean

ROBERT HEFNER, a natural-gas magnate, feels vindicated. As the head of GHK Exploration in Oklahoma, he has been telling people for years that America abounds in gas. But as recently as two years ago the conventional wisdom was that America was running out of the stuff, and investors began considering building new terminals to import the liquefied form from abroad. All that has now changed. "I used to say we were awash in gas," says Mr Hefner. "Now I say we're drowning in it."

The big news is that in June the Potential Gas Committee, a semi-official body, revised its estimates of America's gas reserves, raising them 39% above its assessment in 2006. The biggest part of that boost comes from higher estimates of gas in shale formations, which were formerly difficult and expensive to reach. Advances in horizontal drilling and the hydraulic fracturing of rock have made it possible to get previously inaccessible gas out. Shale gas, according to the committee, accounts for two-thirds of America's technically recoverable reserves, enough to supply the country for 90 years.

This gas may not flow right away. Although oil prices have shot back up since last year's collapse, natural-gas prices, which fell with oil's, have stayed low. The average price in July of $3.50 per thousand cubic feet would be equivalent to roughly $21 per barrel of oil. (West Texas Intermediate oil now fetches $70.) This is too low to sustain much exploration and drilling. But as the economy recovers, and with it demand for gas, prices should bounce back.

More surprisingly, in a season of bitter political argument support for natural gas has become bipartisan. It has hooked those on the right who like the fact that it is abundant in America (and in friendly Canada). But it has also attracted the centre-left. John Podesta, the head of the Centre for American Progress, a think-tank, and Tim Wirth, a former Democratic senator, came out strongly in favour of gas in a paper published this week.

Gas emits about half as much carbon dioxide as coal per unit of energy produced. Putting a price on carbon dioxide, as the cap-and-trade bill that passed the House in June would do, would make coal more expensive to burn and gas relatively cheaper. This could cut carbon emissions in two ways.

The biggest source of greenhouse-gas emissions is electricity generation. Coal, the cheapest fuel, currently produces America's baseload power: coal-fired plants run constantly to meet basic demand, with natural gas switched on when demand is higher. But gas could play a bigger role: there is a third more gas-powered than coal-fired capacity available. A reasonable carbon price would mean that gas plants would be switched on more often to replace coal. And in the longer run carbon prices will rise under Waxman-Markey, as the House bill is known. This could make gas the preferred fuel for baseload power—and make building old fashioned coal plants uneconomic.

There could also be good news for transport, the next biggest source of carbon emissions. Natural-gas boosters, unsurprisingly, support cars powered by compressed natural gas, noting that gas infrastructure (for stoves and heating) reaches millions of homes and businesses already. Many petrol stations are already hooked up to gas-lines for heating. Electric cars, however, have had more attention from carmakers, and they could be powered by electricity from relatively cleaner natural gas. The hurdles for electric cars are in the electrical grid—currently overloaded, and not ready for a big switch to electric cars—and still-developing battery technology. Some even dream of using natural gas to make hydrogen which would power fuel-cell cars, though advocates admit that these are still a long way off.

Some greens worry that natural gas could hamper the development of renewable energy. But the proponents of natural gas see harmony, not competition, with coal and oil the real enemies. Some foresee hybrid wind-gas and solar-gas plants, with gas producing electricity when sun and wind are weak. Gas has featured surprisingly little in the energy debate so far. But it may yet play a bigger role as the Senate, coming back from recess in September, takes up and modifies the bill.

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The politics of health reform

Friend or foe?

Aug 13th 2009 | NORTH ARLINGTON, NEW JERSEY
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It is not wise for Democrats to bash health insurers

Getty Images



No-one said it would be easy

"I AM not a Nazi, I'm not being paid to be here, and I'm not un-American!" The elderly man who uttered those angry words on the afternoon of August 10th was clearly boiling over. He and several hundred others had gathered in a poorly ventilated hall in North Arlington, New Jersey, to berate Steven Rothman, their Democratic congressman, for advocating health reform. The patriotic constituent echoed the sentiments of the angry crowd by declaring that the Democrats' health plan was something his children and grandchildren simply "can't afford".

With Congress in recess this month, many members are holding such town hall meetings—and meeting a similar reaction. Across the country politicians are being confronted with the outrageous allegation that Democratic reforms will create a rationing bureaucracy of "death panels" to decide who lives and who dies.

What explains all this? The initial Democratic instinct was to see a dark plot masterminded by conservatives. Mr Rothman recalls encountering such open hostility at public meetings only twice before—during Bill Clinton's impeachment saga and over the Iraq war—but the difference this time, he insists, is that the complainers are well-organised. A White House official claims that the protests were the result of a "concerted viral whisper campaign". Nancy Pelosi, the speaker of the House, went so far as to suggest this week that the tactics used by those disrupting public meetings were "un-American."

It is true that e-mails and other documents have surfaced confirming that conservative groups and talk-radio hosts have been fanning the flames of discontent. And prominent Republicans ranging from Newt Gingrich to Sarah Palin have indeed pounced on the issue with glee. The former governor of Alaska even posted a note on her Facebook page claiming that Democratic reforms would somehow do in her handicapped child.

Look beyond such opportunism, however, and it becomes clear that there is much genuine anger and concern among ordinary people about health reform. For one thing, the punters at these meetings often have poignant and unscripted personal tales that explain their distrust of proposed reforms. Also, numerous polls now confirm that scepticism among Americans at large—and independents in particular—is growing about health reform.

The Democrats are using two other strategies to try to quell dissent. The high-minded tactic is the White House's redoubling of efforts to address the concerns of Americans directly. To that end, the administration has set up a new website designed to debunk half-truths and myths and is pouring money into a huge advertising campaign. Mr Obama has also headed out on the road again, with three town hall

meetings on health reform planned for this week alone.

The more underhanded gambit is the decision to bash the insurance industry at every turn. Ms Pelosi now calls its bosses "villains", while Mr Obama wags a disapproving finger. This will score some political points, as many Americans have a deep (and often well-founded) distrust of health insurers. But the tactic could ultimately hobble or even doom reform. That is because the health insurance lobby may prove to be Mr Obama's most important friend this year.

Though it has a shameful history, the insurance industry has done a U-turn of late. It now accepts the need for a radical overhaul of insurance markets through measures such as guaranteed issue of coverage and the creation of health insurance "exchanges". But its leaders are increasingly unhappy about the shrill attacks. Can Mr Obama continue to bash the insurers one day and rely on them the next?

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Helping the auto industry

Swings and roundabouts

Aug 13th 2009 | WASHINGTON, DC
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More money for a favoured scheme

“CASH-FOR-CLUNKERS” is a Democrat’s dream: a policy that simultaneously saves rustbelt union jobs and the environment. It promises Americans up to $4,500 if they trade in a car that gets 18 miles per gallon (8km per litre) or less for a new one that gets at least 22 miles to the gallon. Helping people buy cars, it turns out, is popular. Americans snapped up all of the $1 billion Congress set aside for the programme in its first week. So on August 6th the Democrats cheerfully approved another $2 billion.

But critics argue that the scheme is not so green, pointing to the environmental costs of building new cars and destroying the clunkers (a requirement under the programme). True, many people are buying efficient models; the Ford Focus, the Toyota Corolla and the Honda Civic are currently the programme’s three best-selling cars. But stretched incomes appear to be the reason, as much as government subsidy.

Sales have certainly improved, hitting an eye-popping annualised rate of 19.6m in the last week of July according to Edmunds.com, a car website, though that presumably came at some cost to spending in other sectors of the economy—not to mention used-car lots and car-repair garages. There are signs, however, that the bonanza will be short-lived. Edmunds.com reckons consumers’ intent to buy is already down 15% from its peak on July 29th, as the pool of qualifying car-buyers becomes exhausted. It projects that sales will return to pre-cash-for-clunkers levels by the end of August.

The year after France discontinued a similar programme back in the 1990s, car sales plummeted 20%. If normal demand does not improve before the exceptional sales generated by the scheme come back down to earth, Detroit could find itself on a shakier footing once again. In that case, expect America’s carmakers, and their powerful unions, to push for more market-distorting inducements from Washington, DC.

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Drought in Texas

Not a cloud

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The state is staggering through its worst drought for half a century



CROPS are dying. Throughout central and southern Texas swimmers are being turned away from lakes and pools: the dwindling water supply is for drinking, not splashing around in. In San Antonio people are under strict orders to curb their water use, and if you see your neighbours watering the lawn you are supposed to report them to the police. One town resorted to a prayer service; it got 0.03 inches (0.8mm). In June and July Austin hit triple-digit temperatures on 39 days.

Texas's summer has been unusually hot and dry, and punishingly so. According to the state Department of Agriculture, 77 of Texas's 254 counties are experiencing "exceptional" drought conditions, the worst category going. The swathe spans roughly one-fifth of the state, an area larger than Massachusetts, New Jersey and Connecticut combined.

Agriculture is the business that is hardest hit. Losses are already estimated at $3.6 billion and rising. (Under normal circumstances farmers and ranchers bring in about $20 billion a year.) Travis Miller, an agronomist at Texas A&M University's AgriLife centre, reckons that the people being hurt most at the moment are small cow-and-calf operations. Their forage and water supplies have diminished, but the cattle must still be fed. Smaller outfits seldom have much of a cushion to buy extra feed, and Texas had a nasty drought last summer, too. "It'll rain again, and we'll buy some more cows," says Mr Miller. "But right now we're selling a lot of cows, and selling a lot of calves, and it'll take a while to build that back up."

There is little relief on the horizon. Last year Congress passed a farm bill that provides several billion dollars in relief for losses sustained that year, but those funds will not be disbursed until the autumn. Last month Texas's governor, Rick Perry, issued a disaster proclamation for much of the state, noting that the drought conditions have worsened the threat of wildfires. If the federal government declares a state of emergency, Texas ranchers will be eligible for low-interest loans and other forms of aid. So far the national Department of Agriculture has demurred, though Texans can get their hands on some federal money through a grasslands-conservation programme.

There might, however, be a silver lining. All the water restrictions and conservation measures may have the effect of encouraging Texans to pay more attention to water management. This is a growing concern not just in the Lone Star state but all over America's arid south-west. Amy Hardberger, of the Environmental Defence Fund in Austin, suggests that asking people to stop watering their lawns in the blistering afternoon sun is like asking them to swap their light bulbs for the energy-efficient variety: not a cure-all, but a valuable conceptual lesson. "You can't do the broader-context stuff unless people understand it in their day-to-day lives," she says. Meanwhile, everyone is hoping for a change in the weather.

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Immigration

When home is prison

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Slow improvements in the processing of immigrants

WHICHEVER way they go, Barack Obama's battles for health-care reform and a carbon-trading regime will make it hard for him to tackle any other large issue this year. So it was no real surprise this week when he announced, at a summit with the presidents of Mexico and Canada, that his administration will not pursue immigration reform until 2010 at the earliest. Many watchers were still disappointed. During the campaign Mr Obama said immigration would be a priority, and in April the administration said it would raise the issue this year.

At an annual conference on border security held by the University of Texas-El Paso this week, the president's backtracking was on everyone's mind. David Aguilar, the chief of the federal Border Patrol, said that comprehensive reform would help his agency focus on the more dangerous types of illegal cross-border activity. Bob Filner, a congressman from California, hoped that Congress could at least reach for some "low-hanging fruit" such as the proposed DREAM Act, which would provide a path to citizenship for undocumented adults who were brought to America as children. And Janet Napolitano, the secretary for homeland security, said that she shared the interest in reform; though, for the present, her agency's job was to enforce existing law more intelligently.

Her department has already made changes. The administration has scaled back the workplace raids that were so controversial during the Bush years. It is opting instead to focus on auditing employers and expanding E-Verify, an electronic system that lets employers check the immigration status of potential employees.

But the biggest shift concerns family detention. In 2006 George Bush said he would end a policy known as "catch and release", whereby illegal immigrants were allowed to go free after being caught because so many of them failed to turn up for subsequent court proceedings. But detaining children and families proved more delicate than holding lone adults. Later that year, Immigration and Customs Enforcement (ICE) opened a facility specifically for families in Taylor, a small town north of Austin.

The T. Don Hutto Family Residential Centre was formerly a medium-security prison. In its new incarnation it is still run by the Corrections Corporation of America, a private prison company. And inside, Hutto used to be just like a jail. Barbara Hines, director of the Immigration Clinic at the University of Texas's law school, says that she was shocked when she started visiting: children were wearing prison uniforms and the parents were depressed and desperate. Everyone was cooped up in cells for most of the day, and the children had only an hour or so of lessons.

In March 2007 the Immigration Clinic and the American Civil Liberties Union sued Michael Chertoff, then the head of the Department of Homeland Security, over the conditions at Hutto. In August that year the parties settled, with the government agreeing to a list of reforms. That agreement was set to expire later this month, but on August 6th ICE announced an overhaul of America's approach to detention. As immediate steps, the government would put monitors in many of the adult facilities, and immediately stop detaining families at Hutto.

The announcement raises questions. For one thing, it is not clear where the families are going to go. ICE said that it would move them to the Berks Family Residential Centre in Pennsylvania, but that facility is full. And although Berks is somewhat nicer than Hutto, immigrants'-rights groups are still sceptical about keeping children in detention at all.

Planning large-scale reform next year may still be too ambitious: it is an election year, which makes politicians even more skittish about controversy. But some reform advocates are more optimistic: at least, reckons Charles Foster, an immigration lawyer in Houston, immigration reform is still on the agenda.

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Rich animals

The dog will have his day in court

Aug 13th 2009 | NEW YORK
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Courtroom yapping over Leona Helmsley's estate

Rex Features



Tell me about the money

IN LIFE, she was the controversial "Queen of Mean". In death, it is Leona Helmsley's generosity that continues to make headlines. The billionaire hotelier did not hold a high opinion of her fellow humans; but she did love dogs. In her will she left a $12m trust fund to Trouble, her Maltese, and established the Leona B. and Harry M. Helmsley Charitable Trust, now worth an estimated $5 billion, which she said should be distributed to good causes, showing special preference for the care of dogs. Both these bequests have been struck down in court. Trouble must make do with just $2m, which reportedly pays for a security detail costing $100,000 a year. As for the rest of the canine nation, a judge ruled in February that Helmsley's trustees were free to give the money to whichever charitable causes they saw fit.

On August 11th three leading animal charities said they would seek to overturn the second ruling. The American Society for the Prevention of Cruelty to Animals (ASPCA), the Humane Society and Maddie's Fund (established by the founder of PeopleSoft, a software firm, in memory of his miniature schnauzer) accused the trustees of disregarding Helmsley's express intent, a "blatant abuse of the estate", and of "a disdainful attitude to animal welfare". Of the first $136m in grants doled out by the trustees this spring, only $1m was dog-related. A statement by the trustees, who include Helmsley's brother, two grandchildren, her lawyer and a long-term friend, says: "Did Leona Helmsley intend for this charitable trust to focus on the care and help of dogs, rather than people? Absolutely not."

This will be a hard case to win, and much may depend on the attitude of the state's attorney-general, Andrew Cuomo, who has so far supported the trustees. Will Mr Cuomo, who most analysts reckon wants to be the next governor of New York, maintain a position so upsetting to the state's animal-lovers? The animal groups are going to make a lot of noise about needing Helmsley's fortune to tackle problems such as the 2m dogs being "needlessly euthanised" each year, the rapid spread of illegal dog-fighting, and the potential health risk to humans if animal welfare is not properly funded. If the money doesn't end up going to the dogs, maybe Mr Cuomo's election chances will.

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California's overcrowded prisons

Gulags in the sun

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The consequences of three decades of being "tough on crime"

AP



Cruel and unusual

ALL night they battled. Hispanic inmates on one side, blacks on the other, they smashed glass to use the shards as knives and ripped off pipes for bludgeons, burning down part of the prison and injuring hundreds. The riot on August 8th-9th was not the first and won't be the last in California's dreadful prison system.

It occurred in a prison in Chino, just east of Los Angeles, that houses nearly twice as many inmates as it was built for, about the same degree of overcrowding that plagues California's 33 prisons as a whole. It is also one of the prisons that are currently trying to implement a 2005 ruling by the Supreme Court that inmates must not be segregated by race.

The overcrowding in California's prisons, by far the worst in the country with only Georgia and Alabama coming close, has been the subject of lawsuits for years. The latest riot came just days after three federal judges, calling conditions "appalling," ordered California to prepare, within 45 days, a plan to bring its prison population down to 137% of capacity in order to approach constitutional standards of decency. Jerry Brown, California's attorney-general as well as a former governor and likely candidate for governor, has vowed to fight the order.

In the past three decades, California's penal system "has gone from one of the best to one of the worst in the world", says Joan Petersilia, an expert on prisons at Stanford Law School. In the 1960s and 1970s, California was a model for its success in rehabilitating criminals.

But in 1976 California decided to switch from "indeterminate" to "determinate" sentencing. The first system, emphasising rehabilitation, gives a lot of discretion to parole boards, who can reward good behaviour and also help with overcrowding by reducing inmates' prison time. Determinate sentencing, on the other hand, reflects a philosophy of deterrence and means that prison time is relatively fixed, whether an inmate behaves well or badly.

Since then, California has passed around a thousand laws mandating tougher sentencing. Many have gone through the legislature, where politicians of both parties compete to be "toughest on crime". Others have come directly from voters, who often bring a "crime-of-the-week mentality" to the ballot box, says Barry Krisberg, the president of the National Council on Crime and Delinquency, a think-tank in Oakland.

The result is a disaster, says Ms Petersilia. California spends $49,000 a year on each prisoner, almost

twice the national average. But it still has the country's worst rate of recidivism, with 70% of people who leave prison ending up back in it, compared with 40% in America as a whole.

The new prisons built in the 1990s to help accommodate the prisoners serving these tougher sentences have also helped contribute to the state's fiscal crisis. Last month's desperate deal between the governor and the legislature to balance the budget includes cuts of $1.2 billion from prisons, but many Republicans are objecting to the implication that 27,000 prisoners will have to be released to make these savings. For the time being, California's prisoners remain crammed together—with predictable results.

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Brazil's foreign policy

Lula and his squabbling friends

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A bold Brazilian attempt to integrate South America has run into difficulty. Critics at home say Brazil should put national interest over leftist ideology

Illustration by David Simonds



WHEN the leaders of the Union of South American Nations (UNASUL in Portuguese), a 12-country group inspired by Brazil, met in Ecuador's capital, Quito, on August 10th, there was little spirit of union. Their meeting followed a row between Venezuela and Colombia, whose president, Álvaro Uribe, did not attend, in part because Ecuador broke off diplomatic relations with his country last year.

Hugo Chávez, Venezuela's president, backed by his allies, Bolivia and Ecuador, wanted to condemn Colombia for granting facilities at seven military bases to the United States, which is helping it battle guerrillas and drug-traffickers. "Winds of war are blowing," he thundered. Four countries, including Chile and Peru, backed Colombia. Brazil's president, Luiz Inácio Lula da Silva, tried to damp down the dispute, suggesting that the group meet both Barack Obama and Mr Uribe to seek reassurances about the use of the bases. But then Mr Chávez launched a diatribe against Colombia and Mr Obama. Lula cut short his visit to Ecuador and headed home, giving warning that UNASUL could "cease to be an integration process, becoming just a group of friends." If only.

This fiasco provides fuel for both sides in a long-running debate in Brazil about the foreign policy of the Lula government. The critics, who include several senior former diplomats, accuse the government of placing ideology above Brazil's national interest—especially in policy towards South America.

Lula's predecessor, Fernando Henrique Cardoso, sought to boost trade and other ties with the United States and Europe. On taking office in 2003, Lula placed new stress on south-south ties. Brazil has doubled the number of its embassies in Africa, to 30, and joined or set up a clutch of new clubs. These include IBSA, with India and South Africa, of which Itamaraty, the foreign ministry, is especially proud.

As evidence that this policy has borne fruit, Celso Amorim, the foreign minister, points out that most of Brazil's trade is now with developing countries, thus anticipating Mr Obama's advice that the world should not rely on the United States as consumer of last resort. He concedes that Brazil does not agree with the other big emerging powers on everything, but they do share an interest in trying to change the way that

international institutions and the world economy are run.

The critics see in some aspects of the government's diplomacy an implicit anti-Americanism. Lula got on well with George Bush even while disagreeing with many of his policies. Brazil's relations with the United States are correct, but oddly distant. Lula retains a soft spot for Cuba, perhaps because Fidel Castro helped him and his party when they were struggling against a military regime which, at its outset at least, had American backing.

But the anti-Americanism comes from some aides more than from the president himself. He has promoted ultranationalists within Itamaraty. He gave responsibility for South America to Marco Aurélio Garcia, the foreign-relations guru of his Workers' Party. This was one of Lula's many balancing acts, compensating his left-wing base for its disappointment that he ignored them on economic policy.

Brazil has successfully led the UN mission to stabilise Haiti. But in Lula's first term his advisers seemed to think they could integrate South America, against the United States and from the left. Several South American countries do not share their anti-Americanism. (One former Lula adviser derides them as "boy scouts" and as the equivalent of the collaborationist Vichy regime in wartime France.)

Brazil embraced Hugo Chávez's Venezuela, inviting it to join the Mercosur trade block. The naivety of this approach became apparent when Bolivia, at Mr Chávez's urging, nationalised the local operations of Petrobras, Brazil's state-controlled oil company. In what has been called the "diplomacy of generosity" towards left-wing governments in its smaller neighbours, Brazil agreed to pay more for Bolivian gas. Last month it similarly agreed to pay Paraguay more for electricity from Itaipu, the hydroelectric dam they share.

By common consent, policy towards South America has become more pragmatic in Lula's second term. In particular, Brazil's relations with Colombia have improved. Brazilian diplomats say privately that their aim is to contain and moderate Mr Chávez. But Lula has often seemed to endorse him. Would Brazil ever criticise Mr Chávez for endangering democracy? "It's not the way we work," says Mr Amorim. "It's not by being a loudspeaker that you change things." Yet Brazilian officials were not shy about criticising Colombia's military agreement with the United States.

Their critics argue that Brazil should seek to integrate South America on the basis of rules, rather than political sympathy, and that by proclaiming regional leadership it risks becoming the target of regional grievance. They also question the utility of UNASUL and its first project, a South American Defence Council. "To defend against what?" asks Mr Cardoso. Brazil's armed forces did not propose the defence council, nor do they see the American presence in Colombia as a threat. "The United States isn't attacking Latin America. Chávez threatens, he's not being threatened," says Mr Cardoso.

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Football and politics in Argentina

Hand of gold

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Another government bail-out

BETWEEN them, Argentina's president, Cristina Fernández, and her husband and predecessor, Néstor Kirchner, have nationalised their country's post office, its airline and the private pension system. Now, it seems, it is the turn of football to come under the state's aegis. This week the Argentine Football Association was poised to accept an offer of $154m from the state television channel for the rights to transmit this season's matches. The association's president, Julio Grondona, unilaterally ripped up a contract lasting until 2014 under which Torneos y Competencias (TyC), a private broadcaster and partner of the Clarín media group, paid $70m a year for the lion's share of the broadcasting rights.

Nobody disputes that Argentine football is a mess. Many of the brightest Argentine stars play for much bigger salaries in Europe, so many clubs field teams made up of youths and veterans. Despite this transfer income, mismanagement and corruption mean that many of the clubs are shouldering big debts, including $8m in unpaid wages to players and $80m in taxes. That prompted Mr Grondona, who has ruled Argentine football with an iron hand for 30 years, to threaten to suspend indefinitely the new season's kick-off, scheduled for August 14th.

The Kirchners fared poorly in a legislative election in June. Ms Fernández's government lost its majority in the lower house of Congress, while Mr Kirchner was humiliated by coming second in the election for deputies in Buenos Aires province. Opponents claim that the new television deal was crafted personally by Mr Kirchner to restore his political fortunes.

First, he would be seen as the saviour of the season, as well as the man who put football on free-to-air television (though cable, on which TyC is available, is widespread in Argentina). Second he would strike a blow against the Clarín group, whose newspaper has been critical of him. TyC's president claims that Mr Kirchner persuaded Mr Grondona to switch the contract at a late-night meeting, and says he will sue the association. Officials later denied that the meeting took place.

Football and politics have rarely been far apart in Argentina. When the World Cup was held there in 1978, the country's then military junta is alleged to have arranged to bribe an opposing team to ensure Argentina's progress and eventual victory. To curry public favour, the junta also stooped to abolishing relegation when popular teams were threatened with demotion to a lower league.

Mauricio Macri, the mayor of Buenos Aires, built his reputation by successfully running Boca Juniors, one of the capital's two big clubs. Such jobs are hotly contested, despite the clubs' poor financial state. Buenos Aires is plastered with posters for rival candidates in an election for the presidency of River Plate, Boca's big rival. Whoever wins may now command a bigger pot of television money—courtesy of the taxpayer.

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Energy v environment in Canada

Bombs in the bush

Aug 13th 2009 | VANCOUVER
From The Economist print edition

A gas boom triggers rural resentment



SOMEONE is disturbing the peace in the remote Peace River country of British Columbia. Since last October six bomb attacks have been made on natural-gas pipelines near Dawson Creek by someone demanding that their operator, EnCana, dismantle them. Nobody has been hurt and the damage has been minor, but the risk of a huge explosion is great. The latest bomb, on July 4th, caused a leak 500 metres from where workers were repairing damage from another attack three days earlier. In a letter to a local newspaper the bomber gave EnCana until mid-October to commit to a five-year plan to cease operations in the area, or face larger attacks. EnCana has responded by offering a C$1m ($920,000) reward for information leading to the arrest of the saboteur.

Long a bucolic place of fertile farms, the Peace valley has become the centre of the hottest natural-gas boom in North America. New drilling technology has unlocked two vast pockets of shale gas with recoverable reserves of about 70 trillion cubic feet (2 trillion cubic metres). A stampede of energy companies has snapped up exploration rights, drilling more than 700 wells last year alone, and building pipelines. They have brought a bonanza of jobs and wealth to the area and to the province. In 2008 the provincial government netted C$2.66 billion in sales of land and drilling rights, and a further C$1 billion in royalty payments.

To the mysterious bomber this represents the destruction of a rural arcadia. The police take the threat seriously. They have beefed up local units and called in a national counter-terrorism squad. A decade ago more than 160 sabotage attacks took place in next-door Alberta, in protest at the energy companies' alleged disregard for farmers, and particularly their practice of flaring gas to eliminate toxic impurities. This was blamed for causing stillbirths in animals and humans. The police have interviewed one of those responsible for that outbreak of vandalism (who was jailed for two years) but have eliminated him from the current investigation.

According to Paul Joosse, a sociologist at the University of Alberta, the latest bomber, who he believes is either an angry landowner or disgruntled EnCana employee, has tapped the locals' resentment at the disruption to their way of life. The energy boom has inflicted extra traffic on their roads and, say some, seen property rights trampled, while many of the benefits go to the cities. As well as catching the bomber, the authorities have some community work to do.

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More bricks in the wall around her

Aug 13th 2009 | BANGKOK
From The Economist print edition

The junta cocks another snook at the Burmese people and foreign opinion

Reuters



THE only surprise was that it took so long. After many delays, a court in Yangon this week delivered its verdict on Myanmar's opposition leader, Aung San Suu Kyi. The ruling junta's staunchest foe was consigned to another 18 months of detention at her home, as punishment for a bizarre incident in May when an American eccentric swam to her lakeside villa. This, the court ruled, broke the terms of the house arrest she was already serving. Her reasonable defence, that as a prisoner she was in no position to fend off uninvited visitors, was brushed aside by the court.

The pretext provided by the hapless visitor, John Yettaw, a 54-year-old Mormon, may have been fortuitous. But the outcome was never in doubt. The junta was always determined to prolong Miss Suu Kyi's detention, which was about to expire, until after elections that are planned for some time next year. At large, Miss Suu Kyi, who is probably as loved as the generals are hated, would jeopardise this tightly controlled exercise. The last time the regime held an election, in 1990—when she was already locked up—her party won over 60% of the votes and 80% of the seats. The results have never been honoured.

This week Miss Suu Kyi's initial sentence was for three years' hard labour. But in a carefully choreographed intervention, the interior minister promptly stood up to announce that the junta leader, General Than Shwe, had magnanimously commuted it. By giving a gentler sentence he may hope to minimise international outrage. Another explanation was hinted at by Miss Suu Kyi's lawyer, who suggested the act of clemency might also complicate the appeal she is to make against the verdict. At the very least, the manner in which Than Shwe directed her trial is a reminder, if one were necessary, of how completely the armed forces control all of Myanmar's institutions. The whole country is a prisoner of the regime.

Mr Yettaw, who testified he was motivated to make his swim by a vision in a dream, was told to serve four years' hard labour and three years in prison. Aung Naing Oo, a Burmese scholar at Chiang Mai University in Thailand, suggests that the regime will be keen to expel him sooner than that. The generals probably do not want Bill Clinton pitching up in Yangon, as he did in North Korea, to appeal for mercy.

The trial has given the opposition, many of whose leaders are in exile or in jail, some publicity. It has provoked routine international condemnation and calls from activists and others for an arms embargo and

further sanctions. Yet it is doubtful that much will change. Myanmar already faces Western sanctions, while enjoying trading links with Asian neighbours. The country can rely on Chinese and Russian support in the United Nations Security Council, so harsh new measures against the regime—even an arms embargo—are unlikely. When the UN's secretary-general, Ban Ki-moon, visited Myanmar in July to beg the generals to free Miss Suu Kyi and other political prisoners, they simply ignored him. This week the Security Council could not even agree on a statement criticising the verdict on Miss Suu Kyi. As Western and even South-East Asian governments condemned it, China urged the world to respect Myanmar's laws.

Myanmar has been under a military dictatorship since 1962 and the generals' grip looks as strong as ever. Nonetheless, the planned general election raises the tantalising possibility that politics could change. Although the armed forces will remain supreme, the new administration will have a civilian face. The election will be neither free nor fair—it is not even clear how candidates will be selected—yet the establishment of a new system could still amount to the greatest upheaval in domestic politics since the army seized power. The most optimistic analysis is that the new arrangements offer the remote possibility of some change for the better, even if that is not their architects' intention.

Outsiders may have more to worry about than the lack of democracy in Myanmar, however. Last month Hillary Clinton, the American secretary of state, while in Thailand for a security conference, suggested that Myanmar may be receiving assistance from North Korea in building nuclear weapons. Defectors speaking to Australian researchers have alleged that an elaborate nuclear programme is being concealed in tunnels. If such suspicions persist, that issue may come to shape American thinking on Myanmar at least as much as the persecution of Miss Suu Kyi and other unfortunate democrats.

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Afghanistan's presidential election

Incumbent on him

Aug 13th 2009 | KABUL
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Hamid Karzai seems poised for a victory few will cheer



KICKING up dust in Kabul's main stadium, to a tinny background noise of Persian poetry and Muslim prayer, 10,000 Afghans gathered on August 7th for a rare glimpse of their president, Hamid Karzai. It was brief, too. Mr Karzai, wearing the motley tribal garb that made him, in more hopeful times, a symbol of national unity in a war-shattered land, arrived in a scrimmage of foreign photographers, spoke for ten minutes and then was bundled away.

As almost his first campaign appearance in Kabul, ahead of presidential and provincial elections due on August 20th, this was underwhelming. The crowd was mostly of Hazaras, members of an organised Shia community. It included relatively few Pushtuns, members of Afghanistan's biggest group and Mr Karzai's own, from which Afghanistan's Taliban insurgency is drawn, or Tajiks, the second-biggest—and those present seemed unenthused. "In seven years, Karzai has given us no jobs, no factories and outside Kabul there is no security," said Abdul Raouf, a Tajik carpenter.

Many Afghans are disenchanted with Mr Karzai, who has ruled since America bombed the Taliban from power in 2001; he was elected president in 2004. Yet until last week he had hardly campaigned, relying instead on the absence of a popular Pushtun rival and deals brokered with non-Pushtun toughs. These include Mohammad Muhaqeq, the main Hazara strongman, Rashid Dostum, a feared Uzbek warlord, and Mr Karzai's forbidding Tajik running-mate, Mohammad Fahim. Mr Karzai has also enlisted as an adviser Abdul Rasul Sayyaf, an Islamist militant who welcomed Osama bin Laden to Afghanistan in 1996. These choices have not delighted the already disaffected donors who prop up Mr Karzai's corrupt regime.

His main challenger, Abdullah Abdullah, a former foreign minister of mixed Pushtun-Tajik blood (but considered Tajik), has campaigned hard. Allegedly flush with Iranian money, Mr Abdullah has held rallies across Afghanistan, including the insurgency-ridden south. Unlike the president, Mr Abdullah and another candidate, Ashraf Ghani, a former finance minister with strong American but little Afghan support, have proposed interesting policies, including during a televised debate from which Mr Karzai backed out. To correct this, the president was expected to take part in another debate on August 16th.

Though under pressure, Mr Karzai is still firm favourite to win, if perhaps without an outright majority. That would lead to a run-off between the top two candidates, set for October 1st—assuming they do not, as some pundits predict, instead strike a deal. An opinion poll released this week gave Mr Karzai 45% of decided votes and Mr Abdullah 25%. Among the other 39 candidates, Ramazan Bashardost, an eccentric Hazara who campaigns in a taxi, got 9%, and Mr Ghani 4%.

Yet much about this election is uncertain, starting with Afghans' interest in it. The poll found that two-thirds considered the election "very important". But grizzled Afghanistan hands claim to detect a good deal of apathy, especially in Pushtun areas. Nor is it clear how many Pushtuns will dare to vote: the Taliban and other Pushtun militants have condemned the poll. For extra intimidation, this week saw some spectacular violence. Taliban briefly captured police headquarters in Logar and Kunduz provinces. The electoral commission says around 500 of almost 7,000 voting-stations will be unable to open. But there are many more where observers may fear to tread. A parliamentarian from Helmand says no one will vote outside that violent province's two biggest towns.

That could lead to Pushtun disenfranchisement and fraud. A common belief that the election commission is in league with Mr Karzai reinforces fears of the latter. So has a massive over-registration of voters, especially of non-existent women by their self-declared male relatives. By one estimate, 3m of 17.5m

registered voters are frauds. Yet Mr Karzai looks well enough placed for the final results to be unaffected by rigging, which supporters of many candidates may attempt. If he wins, it is to be hoped that Mr Abdullah’s mostly-Tajik followers concur with the result.

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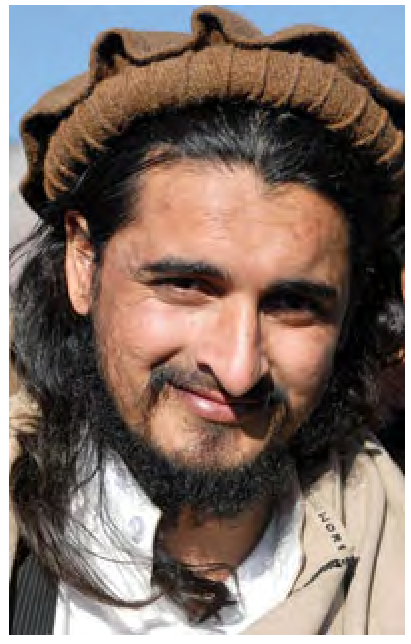
The Pakistani Taliban

Death on the roof

Aug 13th 2009 | LAHORE
From The Economist print edition

A leader is killed, claim his enemies

AFP



The new face of the Pakistani Taliban?

THE tribal areas of Pakistan's borderlands are wild, rugged and impenetrable to most outsiders. So as claim and counter-claim circled this week, it was hard to know for certain what had happened to the leadership of the 13-member coalition of militant groups, the Tehrik-e-Taliban Pakistan (TTP) known as the Pakistani Taliban. It seems likely, however, that a CIA drone attack in South Waziristan has killed its chief, Baitullah Mehsud. According to American intelligence, he was having a "leg massage" on the roof of his house with his second wife when the drone struck. This would be a big victory for Pakistan's campaign against terrorists.

Mr Mehsud had cobbled the TTP together in 2007 out of the forces of fractious tribal warlords, and harboured al-Qaeda fighters. His outfit had killed over 3,000 security officers and captured large swathes of Pakistan's North-West Frontier Province (NWFP). Earlier this year American officials even raised the fear that the TTP could sweep into the plains, besiege Islamabad and grab Pakistan's nuclear weapons.

Last month the Pakistani army at last threw helicopter-gunships, tanks and jet fighters into the battle with Mr Mehsud and rolled his forces back. The Americans, busy in Afghanistan, balked at the idea of opening another front in Pakistan. But they too eventually went gunning for him.

Amid a battle to succeed Mehsud as the TTP's chieftain, some contenders, such as Hakimullah Mehsud (pictured), hotly deny the leader is dead. Rehman Malik, Pakistan's interior minister, insists he is but admits there is no "solid evidence". America says much the same.

Pakistan reports vicious Taliban in-fighting. A meeting of surviving Taliban commanders was said to have ended in a brawl and gunfight. On August 12th, intelligence officials claimed at least 70 people had been killed in a battle between feuding Taliban fighters. Pakistan's army is of course delighted. With the TTP in squabbling disarray, it can expect to cajole disgruntled Taliban contenders to switch sides. The intransigent can be isolated. Others may be asked to join "peace talks".

Certainly, reports of Mr Mehsud's elimination comfort hundreds of thousands who fled the army's campaign against the Taliban in NWFP's Swat Valley and are now trickling back to rebuild their homes. But there may be a different sort of trouble ahead. The American drones and the Pakistani army are getting too close for al-Qaeda and Taliban comfort. More and more people will be tempted to take money to betray the leaders' whereabouts. So al-Qaeda's remnants, hiding in the tribal areas, may move into big cities such as Karachi and Lahore. There they will be safe from the drones; and there is no competent Pakistani intelligence system that can flush them out quickly and stop them from making more mischief.

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Australia's opposition

His own worst enemy

Aug 13th 2009 | SYDNEY
From The Economist print edition

The Liberal leader botches a tricky hand

AT FIRST glance it looked as if Malcolm Turnbull, Australia's opposition leader, had fired a deadly bolt at Kevin Rudd, the prime minister. In blocking the government's legislation on climate change, Mr Turnbull seemed to thwart the prime minister on the issue he has made his signature since leading the Labor Party to power in 2007. Mr Rudd has wanted the scheme, which is to set targets for Australia's carbon-emissions reductions, ready for December's climate conference in Copenhagen. But Mr Turnbull might have thrown a boomerang, making him victim of his own attack.

Mr Turnbull is a lustrous figure in Australian politics. Having entered parliament only in 2004, less than a year ago he took over the leadership of the conservative Liberal Party. He promised to shift the opposition's main party back towards the centre, after more than a decade tacking to the right under John Howard. An ex-journalist and lawyer, who made a fortune in Sydney's business world, Mr Turnbull once led Australia's republican movement. But politics has dulled his sparkle. A poll released on August 10th showed only 26% of voters approving of his performance, a plunge of 18 points since mid-June. Almost four times as many voters prefer Mr Rudd as prime minister. The figures reflect two setbacks, each partly of Mr Turnbull's own making.

In June, Mr Turnbull called for Mr Rudd's resignation, citing a leaked e-mail about a plan to help car-dealers stricken by the credit crunch. The e-mail purported to show that the prime minister's office had asked the Treasury to help a friend of Mr Rudd's. But on August 4th Godwin Grech, a Treasury official who testified about it to parliament, confessed that he had faked the document himself. Mr Grech, it emerged, had shown it on June 12th to Mr Turnbull, who then believed it to be real. Mr Grech has since been hospitalised for depression. A report by the federal auditor cleared Mr Rudd of any wrongdoing.

The "OzCar affair" has dimmed many Liberal parliamentarians' view of Mr Turnbull's judgment. A television profile aired on August 3rd hardly helped: by chance, the cameras were in his office the day the forgery was exposed. Peter Costello, a senior Liberal who once coveted Mr Turnbull's job, has groused about his lack of caution. Divisions have sharpened between the party's centrist wing and the Howard-era hardliners who resent Mr Turnbull's ego and his reformist instincts.

The same divisions have shaken Mr Turnbull's bid to shape the Liberals' approach to climate change. Like the government, he supports a cap-and-trade scheme, allowing polluters to buy and sell permits for their carbon emissions. Such legislation has already passed the parliament's lower house, in June. But conservatives contend the scheme will damage business and farming and send jobs offshore. Wilson Tuckey, one of them, accuses Mr Turnbull of "inexperience and arrogance".

To placate them, Mr Turnbull committed his coalition to voting against the bill when it came before the upper house, on August 13th. This aligned the Liberals with the Greens, who think the legislation too weak, and denied it a majority. The government can reintroduce the bill later this year, then call a general election if it is defeated a second time. Given his coalition's disastrous polling, Mr Turnbull is desperate to avoid that. He says he will negotiate amendments with the government when the legislation returns in November. Even if Mr Rudd's scheme survives then, there is no guarantee that Mr Turnbull's leadership will be so lucky.

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Sri Lanka's post-war local elections

Voting in the empty Tigers' lair

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Elections reveal a country still divided



AFTER a resounding military victory over the Tamil Tigers, Mahinda Rajapaksa, Sri Lanka's president, must have hoped for triumph in the first post-war polls in the scarred north. In the event, low turnout and the unexpected success of a pro-Tiger party jolted the government in the elections on August 8th to the Jaffna municipal and Vavuniya urban councils.

Turnout was 22% in Jaffna (of an unrealistically inflated register) and 52% in Vavuniya. The ruling coalition led by the United People's Freedom Alliance (UPFA) won 13 out of 23 seats on the Jaffna council. But the pro-Tiger Tamil National Alliance (TNA) came second with eight. The UPFA was led by a government minister, Douglas Devananda, whose campaign was well financed.

In Vavuniya, where nearly 300,000 people displaced by the war still languish in government-run camps, the UPFA won just two of 11 seats. The TNA secured five, and will be able to run the council in coalition with the Sri Lanka Muslim Congress, which won one seat.

This is not the outcome the government foresaw when it rejected calls to postpone elections to allow the north time for physical and emotional recovery. The TNA used to be a proxy for the Tigers and took orders from its leader, Velupillai Prabhakaran, who was killed by the army in May. The party was widely thought defunct after the Tigers' rout. Some see its strong performance as a sign of growing anger among northern Tamils at the government's failure to normalise their lives after 30 years of conflict. Initial promises of a political package that would resolve longstanding grievances have fallen by the wayside, having been pushed aside until after a presidential election in 2010.

Somapala Gunadheera, a retired civil servant, said the elections show that the annihilation of the Tigers has not achieved the government's main aim, the building of a united Sri Lanka. Indeed, in Jaffna, TNA leaflets claimed that to vote for the ruling coalition would be to subject the peninsula to rule by Sri Lanka's mainly-Buddhist Sinhala majority.

But, as if to demonstrate the extent of Sri Lanka's political and ethnic polarisation, Mr Rajapaksa's coalition won a massive victory in a provincial council poll held on the same day in Uva in the south-east. The mainly Sinhala province also has a large population of Indian-origin Tamils working in plantations. In that council, the UPFA won more than two-thirds of the seats, with 72% percent of the vote.

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Taiwan's typhoon

Taiwan's disastrous typhoon

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AP

The confirmed death toll in Taiwan caused by Typhoon Morakot, which first hit the island on August 6th, causing the worst floods since 1959, is bad enough. By the middle of this week, over 100 people were reported dead and more than 60 were missing. But there had been fears that 500 people had been buried alive in Hsiao Lin, a village in the wooded mountains of Taiwan's south, and even more in remote neighbouring villages. These eased on August 12th, when almost 1,600 people were found alive by a 25-helicopter search mission. Survivors had not eaten for days and helicopters dropped provisions and began a slow evacuation, hampered by drenching rain. The army says it does not know how many people may have died there. The government faced criticism for not having arranged an evacuation as soon as it heard the typhoon was coming. "We should brace ourselves against typhoons as if they are an invading enemy," said Chu Wen-sen, one of Taiwan's leading water-management experts.

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China and the WTO

Let me entertain you

Aug 13th 2009 | BEIJING
From The Economist print edition

A victory for America's news and entertainment industries

CHINESE trade officials are hardly likely to be quaking in their boots over the ruling announced on August 12th by a World Trade Organisation (WTO) dispute panel. The ruling upheld American complaints that China breaks its trade commitments by the way in which it regulates the import and distribution of foreign publications, films and music.

The officials may reflect that this is, after all, the third time the WTO has ruled against China in just over a year and the other cases—one on imported automotive parts and another on counterfeiting—have not yet led to substantial changes in the way business is done. But the latest ruling adds pressure in an especially sensitive area. It may force China to start untangling the variety of motives behind its persistent effort to control the influx of foreign cultural and information products.

Although China's markets have liberalised hugely over the years, the information-based industries remain something of a special case. Virtually all print and broadcast media are government-run or supervised, and subject to censorship by Communist Party propaganda officials. The internet is closely monitored and a great deal of content is blocked. China's own film producers are likewise kept on a short leash, as are book publishers.

A common view among foreign executives in the news and entertainment fields is that China's complex and maddening regulatory restrictions on the import of their products have served a double purpose: both controlling objectionable content, and protecting local industries. China limits the import of foreign films to no more than 20 each year. It also requires that they be distributed through certain government-run companies. Similar restrictions hamper the distribution of foreign books and magazines.

According to James McGregor, an author and former Beijing-based media executive, the case means China's commercial interests are now bumping up against its propaganda interests. China, he said, was looking at all this with one eye open and the WTO is now telling them they have to look at it with both eyes.

In the case of films, foreign offerings certainly do pose a competitive challenge to home-grown Chinese products. In Chinese cities there is a vast trade, illegal but barely hidden, in pirated DVDs of Hollywood movies selling for about $1. Nor can there be doubt that Chinese cinema-goers would continue buying the rather pricier tickets to the legal versions of those films, even if the yearly limit were lifted.

A more open market for these goods could go a long way towards helping America cut its persistent and politically troublesome trade deficit with China, which in the first half of 2009 ran to $103 billion. But such hopes may have to wait. Ron Kirk, America's Trade Representative, praised the ruling as a significant victory for America's creative industries. But China expressed regret at the ruling and rejected its findings. A spokesman for the commerce ministry said that China's market channels for publications and audiovisual products are extremely open, and that China may choose to appeal.

The WTO's dispute-resolution machinery turns slowly. America made this complaint in April 2007. It was later joined by the EU, Japan, Australia and others. Having taken so long to reach this point, the WTO will take a great deal longer to force compliance, especially if China does appeal.

Mr McGregor, meanwhile, advises China to open up bit by bit on films and other entertainment. Foreign hard-news products, he reckons, can be blocked on other grounds, but entertainment has become a commodity, like toasters or anything else. And besides, thanks to the black market in pirated versions, most urban Chinese have already seen "Sex and the City".

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Banyan

The Burmese road to ruin

Aug 13th 2009
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Once a model for Myanmar's generals of successful autocracy, Indonesia now has even more to teach them

Illustration by M. Morgenstern



IF THERE was ever a role model for Than Shwe, Myanmar's vicious, nutty, reclusive "senior general", it was Suharto, Indonesia's late kleptocrat. Suharto was the senior general who had everything. His fabulous wealth made the greedy Burmese generals look like paupers. His children parcelled out the economy as if it were the family vegetable plot. Feted rather than shunned, he was dubbed "father of development" by his fan club, and even many foreigners agreed: development banks needed him more than he needed them. And he held power for 32 years. No wonder the Burmese junta gazed admiringly at Indonesia.

The two countries do have much in common. Both are fabulously rich in resources—hydrocarbons, minerals, timber. Both reached postcolonial independence by way of Japanese occupation. Both are multiethnic states haunted by the twin spectres of racial tension and a separatist periphery. And both have armies with inflated views of their importance to national survival.

A fine recent book on Indonesia by Marcus Mietzner of the Australian National University* highlights five features of the Indonesian armed forces. Four are also shown by Myanmar's. First is the army's (debatable) view of itself as the main bringer of independence. Second is its disdain for periods of civilian rule in the 1950s, dismissed as chaotic, corrupt and, through the spread of regional rebellions, dangerous to the country's integrity. Out of this disdain grew a third feature, a doctrine known in Indonesia as *dwifungsi*, or dual function, of running the country as well as defending it, and a fourth, the entrenchment of the armed forces in the infrastructure of the state. Last year Myanmar's benighted people were forced to endorse a *dwifungsi* constitution in a referendum. Under it, ludicrously undemocratic elections are to be held in 2010, giving some veneer of legitimacy to the soldiers' unbudgeable heft in parliament and government.

The fifth point, too, may yet apply to Than Shwe. What Mr Mietzner terms the "increasingly sultanistic character" of the ageing Suharto's rule opened up a rift with his fellow generals. When the economy collapsed in 1998 and the threat of anarchy loomed, Suharto looked over his shoulder and found nobody was following him. In the end, dictators, however unpopular, despotic and incompetent, rarely fall because they have too many enemies. They fall because they have too few friends left.

Fall, however, Suharto did, in 1998, disqualifying Indonesia's recent history as a serviceable model for

Than Shwe. But what has happened there since Suharto fell should still interest him for two reasons. The first is that there has been almost total impunity both for the grasping dynasty and the torturing soldiers who guarded it. One obstacle to political reform in Myanmar is the generals' fear of war-crimes trials, truth-and-justice commissions, or perhaps lynch-mobs. Indonesia should offer them hope that political change need not inevitably bring retribution.

But Indonesia is an encouraging example for Myanmar for a better reason, too. Facing multiple long-lived insurgencies, Myanmar's generals fear for their country's unity. In the late 1990s, Indonesians also worried about national disintegration and communal strife. Yet except for tiny East Timor, the country remains in one piece. Moreover, under Susilo Bambang Yudhoyono, just re-elected president, it is politically stable, economically resilient and largely peaceful. All political transitions are bumpy. But Indonesia's has been surprisingly free of turbulence. And the country is showing signs of some political self-confidence. This week it reverted to the timid, "non-interfering traditions" of the Association of South-East Asian Nations (ASEAN), curtailing a gathering in Jakarta of exiled Burmese opposition leaders. But at ASEAN's summit in July, it spoke out for more robust regional human-rights standards and against the Burmese junta.

There are two ways, however, in which the Burmese dictatorship differs crucially from Suharto's. The first is that, whereas Suharto faced only insipid opposition leaders, Than Shwe has a nemesis, Aung San Suu Kyi, who is hugely popular at home and internationally revered. There was something personally vindictive about the Alice in Wonderland trial to which his junta has just subjected her. Not just the proceedings ("sentence first—verdict afterwards") but the supposed crime itself—in effect, being poorly guarded—were beyond ridicule. His intervention to show "clemency" by cutting her sentence was salt in her wounds. The whole farce speaks of Than Shwe's determination at all costs to keep her incarcerated during next year's election. The army will never forget its embarrassment in 1990 when her party trounced the army's candidates. She was already in detention.

The Pyongyang consensus

Second, Suharto's claim to paternity over development was not all hot air. Under him Indonesia achieved average annual economic growth of over 6% for three decades. Inequality was stark, but the benefits of growth were felt by most Indonesians. In Myanmar, a tiny, pampered middle class enjoy luxury hotels, golf and shopping malls in Yangon; the generals bask in comfort in the mountain fastness of Naypyidaw, their absurdist capital. But most of Myanmar's people still toil away as subsistence farmers. Economic collapse is not a risk. There is nothing to collapse.

In this respect, perhaps Than Shwe has, after all, found a new role model. That other vicious, nutty recluse, Kim Jong Il, shows the same almost infinite capacity to let his people suffer to keep him in power and cognac, and has an appealing knack for nukes. However, he exudes neither the durability nor the respectability commanded by Suharto in his pomp—let alone by the popularly elected Mr Yudhoyono, who, Than Shwe's underlings might like to recall, used to be one of Suharto's generals.

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* "Military Politics, Islam and the State in Indonesia: From Turbulent Transition to Democratic Consolidation", Institute of South-East Asian Studies, Singapore

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Fatah and the Palestinians

Fresh faces, old hands

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Don't expect anything too different, too soon, from the new leaders of Fatah

AP



A NEW leadership of Fatah, the biggest and best financed of the Palestinian factions, has emerged from the party congress which finally ended on August 11th in Bethlehem, in the occupied West Bank. The "Old Guard" suffered a decisive defeat by the movement's younger generation in the elections to its main executive body. Fourteen out of 18 men voted onto the party's Central Committee are new, most notably Marwan Barghouti, a popular leader who is serving several life sentences in an Israeli prison.

Another strong contender to the presidency once President Mahmoud Abbas steps down, Muhammad Dahlan, was also elected to an executive post, as were Jibril Rajoub, a former head of the Preventive Security Force, and Tawfiq Tirawi, a former chief of the Palestinian intelligence service. They all represent a new generation of Fatah figures, eager for power—and change. One of the most loathed figures on the Palestinian "street", Ahmed Qurei, a former prime minister whose family company sold cement to Israel which was used for building the much-reviled separation wall, was not re-elected.

Fatah has been at the core of the Palestinian national movement for five decades, but since the signing of the Oslo Accords in 1994 and the establishment of the Palestinian Authority (PA) in Gaza and the West Bank, it has earned a reputation for corruption and cronyism. In recent years it has been losing ground to its militant rival, Hamas. The congress, the first in 20 years, was seen as a long-overdue opportunity to breathe new life into the stagnant organisation. Yet although the delegates succeeded in changing the composition of Fatah's executive organs, the election results are unlikely to lead to the upheaval that many have long wanted.

The new leadership is not expected to shake up the party radically or alter Fatah's position towards the Israelis or the peace process. These supposedly "young" leaders are, after all, already in their 50s, with decades of experience in politics, and largely support Mr Abbas's current policies. Indeed, Mr Abbas himself was unanimously re-elected as head of the party, a post he has held since the death of Yasser Arafat, the founder of Fatah, in 2004.

The charismatic Mr Barghouti is considered the leader with the best chance of reuniting the deeply divided Palestinians. Binyamin Netanyahu's Israeli government is not likely to release him for some time, as he was jailed in 2004 on five counts of murder. But Mr Barghouti's strong win has secured his position as the main contender to the presidency and could lead to increased American pressure on the Israelis to let him out, perhaps as part of a prisoner-swap. And Mr Netanyahu, who favours any strengthening of Fatah at the expense of Hamas as a long-term Israeli interest, may be a little more amenable than he looks. He let virtually all Fatah's delegates attend the congress (a courtesy Hamas did not extend) and in private was generally well-disposed towards its outcome.

However, just as some of the new leaders may endear themselves to the Americans, and even to the Israelis, so the congress's firm commitment to a two-state solution of the conflict and negotiations as a way to peace with Israel will further underline Fatah's ideological rift with Hamas. That organisation does not recognise Israel's right to exist and favours armed resistance. The two factions are supposed to meet in Egypt later this month for another round of unity talks. Few expect any results. The inclusion of Mr Dahlan in Fatah's Central Committee is not likely to help reconciliation. When he ran the Preventive Security Force in Gaza in the 1990s, he led a forceful crackdown on Hamas and has been reviled by the Islamist organisation ever since.

National elections are set for January 2010. The new Fatah leadership will still face a strong challenge from Hamas, but even before the conference in Bethlehem Fatah had been enjoying a surge in popular support in the West Bank. This was due partly to the improved economic situation and also to the increased calm on the streets, attributed to the intensive American training of the PA's security forces. Israel's massive onslaught on Hamas-controlled Gaza earlier this year also seems to have validated Mr Abbas's more moderate approach. "I like Fatah more now," said a young man who was selling roast chicken in the market in front of the Nativity church in Bethlehem. "There are a lot of scary things going on in Gaza. Hamas is crazy. Palestine is Fatahland."

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Iran and human rights

The crackdown

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Allegations of torture against opponents of the president

AP



How to make opponents see reason

WHEN residents of Iran's capital seek escape from its choking smog, they often head for the hills, or rather the barren mountains that soar above Tehran's northern suburbs. But the anxious little crowd gathered at the foot of one of these slopes on a recent morning was not in search of fresh air. Clustered around lists of names pasted on a high concrete wall topped with concertina wire, they were hoping for a clue that some missing loved one might be immured inside, in the hillside complex of cell blocks and interrogation rooms that make up Iran's most notorious prison.

Built in the 1970s to house the shah's political enemies, Evin prison has been much expanded since the 1979 Islamic Revolution. During the revolution's grim first decade, thousands of dissidents were summarily shot in its yards. Iran remains second only to China as a dispenser of capital punishment, a practice that has surged under the administration of President Mahmoud Ahmadinejad. But the victims are, with a few ugly exceptions, mostly convicted criminals rather than political opponents of the regime.

Yet Evin, as well as several of Tehran's lesser detention centres, has been busier than ever in the past two months. By the government's own tally, at least 4,000 citizens have suffered arrest and imprisonment in the fierce crackdown that followed the bitterly contested presidential election on June 12th. The sweeping campaign of arrests has muted, but not silenced, opposition to the polls; millions of Iranians still believe that these were rigged to ensure a return for Mr Ahmadinejad.

According to a spokesman for the judiciary, all but 300 of the detainees were freed within a week of their arrest. One conservative MP, part of a parliamentary committee that visited Evin to investigate conditions, declared that its prisoners received the same excellent food as the minister himself. This would be comforting, except that damning evidence, including testimony from released detainees and admissions from some officials, suggests that many endured appalling crowding in custody, ritual humiliation, starvation, sleep deprivation, vicious beatings and worse. A rival presidential candidate to Mr Ahmadinejad, Mehdi Karroubi, claims that both male and female prisoners suffered brutal and repeated sexual assaults.

The abuse at one jail in the south of the city, Kahrizak, was so bad that Iran's supreme leader, Ayatollah Ali Khamenei, ordered it closed last month, after the revelation that the son of a top aide to a prominent conservative politician was among at least three prisoners who had died there. Though officials claim that the deaths were due to a mysterious virus, the prison director is now himself under arrest, charged with negligence.

By the government's count, the number of those killed during the unrest is fewer than 30, including members of the regime's own *baseej* militia. Claims by some that hundreds may have died appear exaggerated, but opposition politicians, demanding a more thorough parliamentary investigation, have submitted a list of 69 people alleged to have been killed.

Those remaining in jail include scores of former officials, academics, journalists and others, the alleged ringleaders of what prosecutors describe as a vast conspiracy to cast doubt on the vote, and so foment a "velvet" secularist overthrow of the Islamic state. Several hundred are being tried as alleged plotters, in partially televised sessions that have been widely condemned as parodies of justice.

Yet Mr Ahmadinejad's henchmen appear to see enemies even closer to his office. Extending a tactic used

in other ministries during his first term, the president has sacked five senior officers in the powerful ministry of intelligence. Their replacement with loyalists from the Revolutionary Guard, the ideologically zealous parallel to the regular army that also controls the *baseej*, has raised alarm even among conservatives of creeping militarisation. Some analysts speculate that the purge was prompted by resistance from within the ministry to efforts to tar all opposition as part of a foreign plot, with the ultimate aim of crushing the reformists for good.

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Security in Iraq

A return to the bad old days?

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A worrying surge in bombings as the Americans plot their departure

CHAIRMAN MAO laid down the rules for modern guerrilla warfare during the Chinese civil war. "When the enemy advances, withdraw; when he stops, harass; when he tires, strike; when he retreats, pursue," he instructed. Iraqi insurgents seem to be following his advice all too closely. During the American "surge" two years ago they melted away. After the surge peaked they renewed their attacks. And barely a month after Iraqi troops took control of the main towns from the slowly departing Americans, blood is once again gushing down the boulevards.

More than 100 civilians were killed in a four-day period this week and hundreds wounded. Two lorries packed with several thousand pounds of high-grade explosives levelled most of a settlement on the edge of Mosul in northern Iraq. Residents were sleeping on their roofs to escape the summer heat when their houses collapsed beneath them. Meanwhile, bombs in Baghdad targeted day-labourers and pilgrims. Altogether this has been the worst spasm of violence in recent memory. Although the attacks were all confined to the capital and the north, while the rest of the country remained relatively calm, they demonstrated a degree of sophistication that American officials thought the insurgents could no longer muster. The truck bombings are reminiscent of the spectacular attacks staged during the early years of the American occupation.

Nobody has claimed responsibility, but there is little doubt that groups like al-Qaeda in Mesopotamia, as the Iraqi wing of the jihadist movement calls itself, are at work in Mosul. They have largely been on the retreat since the surge started in 2007. Many of their leaders have been killed or captured. They have also lost popular support—but not their tactical cunning.

With the lorry bombs, which killed 35 people, the insurgents achieved several objectives at once. They have forced the already stretched Iraqi army into protecting an even greater area by unexpectedly switching from city attacks to hitting a semi-rural place. They have knocked public confidence in the Iraqi government's capacity to maintain security. And lastly the insurgents are returning to their most successful ploy: baiting an ethnic community until it is so fed up that it hits back, thereby triggering further violence.

Previously the insurgents focused on the Shia. But this group is increasingly turning the other cheek. "Let them kill us," said Sheikh Khudair al-Allawi, the imam of a mosque bombed recently. "It's a waste of their time." The insurgents have taken note, and are switching their attention to the Kurds instead. The bombed houses outside Mosul were under the protection of the armed Kurdish fighters of the *peshmerga.* They have so far stayed out of sectarian fighting. But for how much longer? Political control of the area around Mosul, and the oil beneath it, is in dispute. Kurds and Sunni Arabs both want it, with no compromise in sight. The insurgents are trying to whip up a civil war again, and some are taking the bait. In the hours after the lorry bombing, Sunni provincial lawmakers demanded the expulsion of the *peshmerga* for being ineffective.

The renewed violence is a blow for the prime minister, Nuri al-Maliki. Lacking charisma or a record of delivering much-needed schools and hospitals, he has built his strategy for getting re-elected in national polls next January on the supposed gains in security for war-weary Iraqis. Within hours of the lorry bombings he appeared on national television to reassure them, but not everyone is convinced.

The Americans too are trying to sound positive. But more violence could jeopardise their carefully-laid withdrawal plans. For the moment, those are still on course. Nationwide attacks are now averaging 100 per week, compared with 200 last year. But there is a danger that the failure to find an Arab-Kurdish solution for the disputed land will give the insurgents a perpetual *casus belli*.

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Smoking in Iraq

Butt out, please

Aug 13th 2009 | BAGHDAD
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Imposing the mother of all cigarette bans

AP


More lethal than terrorists

IT'S the health and safety measure Iraqis have not been waiting for. The government in Baghdad last week banned smoking in public buildings. Anyone found lighting up will have to pay a fine equivalent to $4,300, enough to buy 17,200 packs of cigarettes at the local price of about 25 cents. "Do the politicians have nothing better to do?" asks Abu Yasser, as he takes a drag while filling up his car at a petrol station. "My cousin was recently murdered by terrorists, my neighbour was tortured by the police, my electricity is cut for most of the day, the same is true in most hospitals in the city. And they are worried about smoking?"

As soon as parliament ratifies the cabinet-imposed ban, Iraqi smokers will be forced to loiter on street corners exposed to car bombs and 45-degree heat in the summer. But according to a recent study, smoking kills an average of 55 Iraqis a day, compared to a current average of ten deaths daily from terrorist shootings or bombings. So the government argues that it is perfectly reasonable to outlaw smoking on public-health grounds.

Nonetheless, the ban has done nothing to improve the already low opinion many Iraqis have of their democratically elected government. "Bring back Saddam," says a cigarette vendor. "We were free to smoke anywhere then." Others link the ban to reports of torture in official detention. "Prisons are public buildings, right? So will they now prevent guards from stubbing out cigarettes on the arms, legs and backs of inmates?" asks one university student. With nerves jangled from years of upheaval, nicotine is often the first and only comfort. Stuck at checkpoints, Iraqis pass around cigarettes. Faced with recalcitrant bureaucrats, they do the same.

In parliament though, the ban is popular. Islamists want to get rid of tobacco outright. Of course, many ministers and MPs smoke too, often in their offices. But, given their elevated positions, few rules apply to them.

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Ethiopia's resilient prime minister

The two sides of Meles Zenawi

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A long-lasting leader faces growing problems at home and abroad



HE HAS run Ethiopia as prime minister since 1991, but Meles Zenawi, still only 54, has two faces. One belongs to a leader battling poverty. In this mode he is praised by Western governments, with Britain to the fore, for improving the miserable conditions in the countryside, where 85% of Ethiopia's 80m-plus people live. Mr Meles takes credit for building new roads, clinics and primary schools, and for an array of agricultural initiatives. He also wins plaudits for his country's low crime rate and for keeping its parliamentarians more or less on the straight and narrow, especially in terms of wealth. They get paid only about $3,240 a year compared with the $120,000 earned by Kenya's fat-cat MPs. Moreover, in the past few years Ethiopia's economy has grown fast. Mr Meles says it will grow this year by 10%, though the IMF's figure is about half as big.

His mind is sharp, his memory elephantine, and he bristles with energy and vigour. In a rare interview, he speaks for two hours without notes. With his polished English, full of arcane turns of phrase from his days at a private English school in Addis Ababa, the capital, he captivates foreign donors. Though he avoids mentioning famine because the spectre of it may be looming again, he uses the memory of past debacles to prick Western consciences. Last month he suggested that the famine of 1984, which stirred Band Aid to come to Ethiopia's help, may have been worsened by the pollution in Europe. He says he fully expects the West to pay $40 billion a year to Africa to compensate it for the damage caused by climate change.

But then there is the harsher side of Mr Meles, the Marxist fighter turned political strongman with a dismal human-rights record who is intolerant of dissent. In 2005, after a disputed general election, his police shot dead some 200 civilians. An independent inquiry ended up with several of its judges fleeing the country. Mr Meles sprinkles spies through the universities to intimidate and control the students; he was once a student agitator himself. He closes down independent newspapers and meddles in aid projects, banning agencies that annoy him. Last month he suspended the activities of about 40 of them from the Somali-populated parts of the country.

Many of Ethiopia's opposition leaders were imprisoned after the election of 2005 on trumped-up treason charges; after a year or more, they were freed. But several have been rearrested. A new catch-all law that has just been passed could make peaceful opposition liable to the charge of inciting terrorism.

In any case, the economic story is not quite as rosy as Mr Meles suggests. Ethiopia may have only a few weeks of foreign reserves left. On the business front, the country remains very backward. Ethiopians have one of the lowest rates of mobile-phone ownership in Africa. Banking is rudimentary at best. Farming is still mostly for subsistence.

And famine looms once more. At that suggestion, Mr Meles narrows his eyes and growls, "That is a lie, an absolute lie." There is more than enough food in government warehouses to feed the people, he says. But others say stockpiled grain has already been earmarked for handing out to people in the towns. The UN and foreign charities are predicting a large-scale famine in Tigray, Mr Meles's home region, by November. At least 6m people may need food handouts unless more supplies can be found locally.

Mr Meles's officials, most of them still working in gloomy Soviet-built offices, often sound almost paranoid in their sensitivity to criticism. The prime minister is quick to talk up threats to his country, whether from malcontents in the army or disgruntled ethnic groups among Ethiopia's mosaic of peoples. Radical Oromos, a southern group that makes up about a third of Ethiopia's people, often fall under suspicion. A bunch arrested earlier this year after an alleged attack on a dam under construction were paraded on

state television as members of the secessionist Oromo Liberation Front (OLF). The government also regularly publicises threats by the Ogaden National Liberation Front, a Somali separatist group in the east, which has murdered foreigners and Ethiopians exploring for oil in that area.

Mr Meles is understandably worried by events in the wider region. Ethiopia's relations with Eritrea, his mother's birthplace, remain lousy. He accuses it of backing jihadists bent on hurting Ethiopia. He also accuses Eritrea of egging on Oromo rebels in the south and Somali separatists in the Ogaden region. "Eritrea is hellbent on destabilising Ethiopia," he says. "It does not care who it sleeps with."

And he remains edgy about the continuing strife in Somalia. In late 2006, with American encouragement, he sent his army there to topple an Islamist government that had declared a holy war on Ethiopia. Earlier this year he withdrew his troops after it became apparent they could not impose peace. But now the jihadists are gaining ground there again, bringing in al-Qaeda types—just what Mr Meles wanted to prevent.

So Mr Meles is up against it, at home and abroad, but apparently relishing the challenges. A general election is due next year. He had previously hinted he might step down after it. More recently, he has sounded less sure, dismissing such speculation as "boring". Some say he may leave his prime ministerial post but stay on to chair his ruling Ethiopian People's Revolutionary Democratic Front. He seems likely, in whatever guise, to call the shots—with decreasing dissent.

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America and Africa

Hillary (not Bill) on safari

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The secretary of state tries to walk all that mellifluous Barack Obama talk

DOUBLE-acts are more common in light entertainment than high politics. But if Barack Obama delivered the punchline of his administration's vision of Africa on his triumphant, albeit very brief, visit to Ghana last month—declaring that "Africa's future is up to Africans"—Hillary Clinton has been trying to put the meat of detail on to the bones of his oratory.

Journeying to seven countries in 11 days, her tour of the continent (the earliest point in any administration that a president and secretary of state have both visited Africa) took in America's varying, and sometimes competing, priorities. Security and the dangers of Islamist terrorism were highlighted in east Africa, democracy in Kenya and Angola, trade in South Africa, oil in Angola and Nigeria, conflict in Congo and HIV/AIDS almost everywhere.

It is a contradictory mix to manage. In Ghana, Mr Obama had spoken of the importance of democracy, of how "governments that respect the will of their own people...are more successful than governments that do not", and the risks of concentrating wealth in the hands of an elite few. His presence in Ghana, rather than in Kenya, where his father was born, was a recognition of the country's peaceful changes of power at the ballot box.

However, given the realities of America's interests, Mrs Clinton could not afford such gestures. Angola has not held a presidential poll since 1992, when the second round was cancelled as the country's civil war restarted. Last month the government, largely composed of former Marxist guerrillas, delayed the next such election for an 18th year when it extended work on its new constitution. Yet America has been investing a lot of diplomatic and political effort in Angola, not one of its traditional allies on the continent, because of its oil. Angola's vast natural resources have seen it boom, with growth averaging 18% in recent years, even though many of its people still live in dire poverty. It is now the biggest oil producer in sub-Saharan Africa.

As such, it has become one of the most keenly contested diplomatic battlegrounds on the continent. Mrs Clinton arrived in the wake of a visit by the Russian president, Dmitry Medvedev, in June and a steady stream of guests from Beijing. Unlike her Asian rivals, who never publicly criticise African regimes, Mrs Clinton at least spoke of the need for a "timely" presidential election to follow last year's parliamentary vote. But otherwise it will be business as usual. Francis Kornegay of the Institute for Global Dialogue, a think-tank based in South Africa, describes the Obama administration's approach in Africa as "progressive realism". "There's no such thing as a human-rights foreign policy, we are in an age of competitive economic diplomacy in areas of the world where we have major concentrations of resources," he says.

In Kenya, with less at stake commercially, Mrs Clinton scolded the government for its failure to bring charges against any politician for inciting violence during the disputed election in December 2007. But she was short on specifics as to what Kenya should do next.

She was also worryingly vague on Somalia, a perennial problem for America. A meeting with Somalia's embattled transitional president, Sharif Ahmed, in Kenya ended with a photo-opportunity in which a nervous Mr Ahmed shook hands with Mrs Clinton in front of the Stars and Stripes. Mrs Clinton hinted that drones would return to the skies over Somalia if the Islamist radicals who now control most of the country launch suicide attacks against Kenya and elsewhere. American officials privately suggested that they would increase the supply of weapons to Mr Ahmed's feeble government.

However, whereas that might be just enough to provoke those who see Mr Ahmed as nothing more than an American lackey and a turncoat, it won't be nearly enough to stop Somalia's further descent into chaos and self-destruction. Away from Mr Obama's rhetoric, such are the real dilemmas and difficult choices for America in Africa.

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Correction: Bahrain

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On the map in our special report on the Arab world (July 25th) we showed the population of Bahrain as 2.8m, GDP as $43bn and GDP per person as $15,000. In fact Bahrain's population is 0.8m, GDP is $18bn and GDP per person is $22,800. Sorry. This error has been corrected online.

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Southern Italy's ills

The messy mezzogiorno

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A political row brings new attention to Italy's neglected, but still troubled, south

Eyevine



THERE was a time when the problems of the Italian south, the *mezzogiorno*, seemed urgent not just for Italy but for all of Europe. Then new members with even poorer regions joined the European Union and the issue slipped off the agenda in Brussels and Rome. Silvio Berlusconi's government does not even have a minister for the *mezzogiorno*—the peninsular south, plus Sicily and Sardinia. Yet the region's problems have not gone away. It matters: the south accounts for a third of Italy's population, half its unemployment and an immeasurable share of organised crime. Now the south is again a hot political issue, with more recent news coverage even than the prime minister's sex scandals.

The trouble began when a group of southerners nominally loyal to Mr Berlusconi threatened to found a new party of the south, along the lines of Umberto Bossi's truculent Northern League. Some were members of a small Sicilian party in the ruling coalition. But the rest came from Mr Berlusconi's own People of Freedom (PdL) movement. As the prime minister himself said, having spent years trying to shoehorn the right into a single party, a split within it is the last thing he wants.

The threatened revolt was staved off by a promise to unfreeze €4 billion ($5.7 billion) in funding for Sicily. It may just be a sign that sex scandals have weakened Mr Berlusconi's authority. But it also reflects southern irritation at the Northern League's hold over the government. Pietro Busetta at Palermo University suggests that the league is creating its mirror image in the south. "Its drive for autonomy pushes people inexorably into thinking that staying together [with the rest of Italy] is worse than being apart."

What brought matters to a head was the discovery that Giulio Tremonti, the PdL finance minister (and a close ally of the Northern League), had raided funds earmarked for development of the *mezzogiorno* to contain a gaping budget deficit. (Public borrowing in the first seven months of 2009 was 140% higher than in the same period of 2008.) Luca Bianchi, deputy director of Svimez, an association for the development of the *mezzogiorno*, estimates that, of €63 billion initially set aside, only a third survived what he calls the treasury's *scippo* (bag snatch).

Italians sometimes talk as if the gap between the north and south were uniquely wide. In fact Spain and Belgium have similar differences. GDP per head in the *mezzogiorno* is almost as high as

Israel's (though below that of any country in the old EU 15). In 2007 Gioia Tauro in Calabria overtook Algeciras in Spain to become the busiest container port in the Mediterranean; and a striking commercial and leisure centre designed by Renzo Piano was added to an immense freight complex at Nola, near Naples. Some of Italy's best wine now comes from Sicily. Some of its most sophisticated tourist destinations are places like Matera in Basilicata. And for years the Apulia region has grown at a healthy clip.



Even so the *mezzogiorno* still has huge problems, which recession seems to be aggravating. Whether the regional gap is growing or shrinking is itself a matter of dispute. According to Svimez, over the past seven years the economy in the south has grown more slowly than in the north. Yet its figures show GDP per head rising compared with the Italian average. That, says Mr Bianchi, is merely because the *mezzogiorno* is losing population. It has a lower birth rate than the north and also has net emigration, particularly of the young and educated. A study last year by CERM, a think-tank, found a "clear preponderance of young men with a high level of education" among those who left.

Other failings are more glaring still. The quality of education in the south is much lower than in the north. A ranking by Shanghai's Jiao Tong university put only three southern universities among Italy's top 20, which are themselves hardly world-class. Infrastructure is often hopeless. It takes five hours to cross Sicily by rail from Palermo to Catania. How long it takes to drive from Salerno to Reggio di Calabria is a matter of chance. Work on modernising the A3 highway was due to finish six years ago, but will not now do so before 2011. The airport at Reggio could almost be in one of the poorer parts of South-East Asia. There is still no physical link between the mainland and Sicily, home to one in 12 Italians—and there remains much scepticism about the wisdom of the Berlusconi government's promised bridge.

"It is not just that the image of the *mezzogiorno* has deteriorated nationally and internationally. There has also been a loss of self-confidence," concludes Alessandro Laterza, a publisher in Bari who is head of the local branch of the employers' federation, Confindustria. The brain drain is one of several factors that make the *mezzogiorno*'s prospects dimmer than those of southern Spain, say. Another is its inability to attract significant foreign direct investment. The entire *mezzogiorno* gets a mere 1% of Italy's already low share of such investment.

Perhaps the biggest concern of all is the pervasiveness of organised crime. Police in Sicily have recently dealt a string of devastating blows to the Mafia, called the Cosa Nostra. But Calabria remains firmly in the grip of the 'Ndrangheta, and Naples and its surrounding region of Campania are still in thrall to the Camorra (see article). Organised crime bleeds healthy firms of cash they might otherwise spend on investment or R&D. And it reinforces the league's argument that spending money on the *mezzogiorno* is pointless because it goes to mafiosi and corrupt politicians.

Northerners' reluctance to see their taxes go south lay behind the league's campaign for more fiscal federalism. The principle was written into the constitution this year, but will take years to implement. Initial southern hostility to the idea has given way to a more receptive attitude to the league's argument that it would foster accountability. Even Mr Bianchi, who suspects that fiscal federalism is unconstitutional, says, "I am convinced it could be an opportunity. Indeed, the south has much more to gain than the rest of the country from federal-style administration."

Mr Laterza agrees. But he notes that a form of fiscal federalism has been tried already. In 1947 five regions, including Sicily, were given extensive powers. "And the experience of Sicily since has been anything but one of accountability," he says.

To hear an audio podcast on the *mezzogiorno*, go to Economist.com/audiovideo/europe

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Iceland and the European Union

The Icesave bill

Aug 13th 2009 | REYKJAVIK
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Opposition to paying back British and Dutch bank depositors is growing

IN RETROSPECT, parliamentary approval to apply for European Union membership was easy. The Icelandic prime minister, Johanna Sigurdardottir, is finding it far harder to persuade Iceland's parliament, or Althingi, to ratify the Icesave agreement her government struck in June.

Icesave was a high-interest, internet-only saving scheme launched by an Icelandic bank, Landsbanki, in Britain and the Netherlands, operating under the EU's single-market rules (since Iceland is a member of the European Economic Area). This meant that, when Landsbanki went bust in October 2008, Icesave depositors were not covered by Dutch and British deposit insurance, relying instead on Iceland's scheme. They also expected to be treated in the same way as Icelandic savers, whose total deposits in Landsbanki were guaranteed by the Icelandic government.

Under the June deal, Iceland, a country of just 300,000 people, is to borrow the staggering sum of $5.5 billion from the British and Dutch governments, at an annual interest rate of 5.5%, to meet the Icesave bill. But an upsurge of criticism from angry voters, who talk of IceSlave and draw parallels with the Versailles treaty imposed on Germany in 1919, is leading the parliament to give the deal a rough ride.

Opponents question both the legality of the British and Dutch claims and the wisdom of taking on so much debt to meet them. Resentment lingers over Britain's invocation last year of anti-terrorism laws to freeze Icelandic assets. And critics say the government has allowed itself to be bullied by the British and Dutch governments just because it is so keen to join the EU.

Ms Sigurdardottir calls the Icesave debate "the most important issue that any Icelandic parliament has been required to address". The government argues that most of the debt will eventually be covered by the sale of Landsbanki assets. It also insists that the deal is an essential part of clearing up Iceland's financial mess. Loans from the IMF and Iceland's Nordic neighbours, worth some $5 billion, are on hold pending its approval. If debate drags on for too long, Iceland's credit rating, already close to junk, could be downgraded again—and that would threaten the chances of a recovery.

Yet by mid-week it seemed unlikely that the parliament would accept the Icesave deal unconditionally. The question was whether it could attach enough strings to satisfy public opinion without undermining the deal altogether. If not, it may jeopardise not only Iceland's EU application—public support for joining has dropped sharply—but also Ms Sigurdardottir's shaky coalition and Icelanders' chances of ever regaining their enviably high living standards.

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Italy's vigilantes

On the beat

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Are the Mafia and the amateur police enemies or allies?

Illustration by Peter Schrank

SPURRED on by the Northern League, many towns in northern Italy have formed officially condoned vigilante groups, rules for which took effect on August 8th. But Rome's mayor believes that crime and public order are best left to the police. And amateur law enforcement by three-man platoons has been greeted even less enthusiastically farther south. Most cities in Campania, of which Naples is the capital, have decided that vigilantes will not patrol their streets.

However, Cipriano Cristiano, mayor of Casal di Principe, a town of 22,000 people a little north of Naples, hopes soon to have two three-man teams in action. The vigilantes will report building and garbage violations, and also illegal immigrants—a dangerous job if done properly. The town and its surroundings are the Casalesi clan's turf. Growing rich on construction and clandestine waste disposal, the clan won worldwide notoriety through the book and film "Gomorra". It lived up to its bloody name in September 2008 when a hit-squad gunned down six Africans in a nearby town, prompting the government to send in 500 soldiers.

Antonello Ardituro, one of an elite team of magistrates investigating the Casalesi, suggests that the clan may place its men among the vigilantes, thus controlling its territory even more closely. "This is a town where officials have colluded with the Mafia," says Marco Del Gaudio, a colleague of Mr Ardituro. In a place untroubled by badly-behaved adolescents, patrolling the streets is risky because so many people carry guns. When Mr Cristiano discusses his plans with the police, they may agree with the magistrates. Where organised crime holds sway (Mr Ardituro and Mr Del Gaudio lead the hunt for two of Italy's most wanted criminals), even the smallest crimes and misdemeanours should be a matter for professionals.

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Germany's Free Democrats

The centre holds

Aug 13th 2009 | BERLIN AND HANOVER
From The Economist print edition

The liberal king-maker of German politics wants its old role back

GUIDO WESTERWELLE is garrulous on most topics. But one he avoids is what job he might have in Germany’s next government. Would he be foreign minister, or perhaps run an economic superministry? Voters care about what the government does, not how the spoils of office are shared out, he responds, with the careful affability of a well-schooled politician.

Mr Westerwelle is cautious because the prospect is tantalisingly near. If the opinion polls are right, his Free Democratic Party (FDP) may oust the Social Democratic Party (SPD) as the coalition partner of the Christian Democratic Union (CDU) after the election on September 27th. That would hugely change the make-up and policies of Angela Merkel’s government.

Although a conservative, Ms Merkel has often leaned left as chancellor. Sometimes she has surrendered grudgingly to her SPD partners, accepting a minimum wage in some areas. Or she has stolen their ideas (eg, aid to working mothers). The pro-market FDP would nudge Ms Merkel towards tax cuts, a more flexible labour market and, by German standards, daring changes in pensions and welfare. The election may turn on whether voters are ready for such a liberal “black-yellow” coalition.

If they are, it would end a painfully long sojourn in opposition for the former king-maker of German politics. The FDP was once part of almost every post-war government, as junior partner of either the CDU or the SPD. But after its eviction by an SPD-Green coalition in 1998, pundits wondered if it would survive. Its decision in 1982 to abandon an alliance with the SPD in favour of one with the CDU triggered an exodus of left-leaning members. Mr Westerwelle, now 47, was one of the few who stayed. After he took over the leadership in 2001 the FDP risked becoming a one-note party, obsessed with tax cuts and at the beck and call of its rich clientele. Its civil-liberties wing was eclipsed.

This is changing. The leadership gap is being filled by a new generation, including Philipp Rösler, the 36-year-old economics minister of Lower Saxony, born in Vietnam and adopted by German parents. Last year he wrote a manifesto calling for the FDP to dedicate itself to “knowledge, tolerance and solidarity”. The party has been too economy and tax-oriented, he says. His generation represents both economic liberalism and social values, he adds.

Leading the FDP into a federal election for the third time, Mr Westerwelle accepts much of this. He now mentions civil liberties almost as often as tax cuts. The FDP’s message is for the “whole nation”, he insists, not just the better off. In 2005 8% of the unemployed voted for the party, not far short of its overall share of 9.8%. The FDP’s social message sounds more like George Bush’s compassionate conservatism than German social democracy. Mr Rösler thinks it is mainly up to society, not the state, to bring about tolerance and solidarity. The FDP still believes that freedom outweighs equality and private initiative is better than public activism.

The biggest surprise of the election campaign so far is how many voters seem to agree, despite capitalism’s worst crisis since the 1930s. The polls predict that the FDP will win some 15% of the vote, which would be its best-ever national score. Mr Westerwelle attributes this to the FDP’s “clarity” and reputation for economic competence, but he has also been lucky. Ms Merkel’s leftward tilt has irked liberals among CDU supporters. Their annoyance has turned to alarm with soaring debt, government bail-outs and threats of expropriation. By backing the FDP, they can rebuke the conservatives without opening the door to a left-wing government.

The FDP would be the “tugboat” in a black-yellow government, says Mr Rösler. Its main demands are a simpler tax system and lower rates for individuals, plus business-friendly changes to corporate tax. Taxpayers would be expected to shoulder more of the burden of providing their own pensions and health care. The FDP would replace a patchwork of welfare programmes with a simple “citizens’ payment”, which could be cut if beneficiaries refused work. It proposes a “re-privatisation board” to reverse the state’s

crisis-driven entanglement in banks and business.

How far the conservatives will allow the FDP to tug them is an open question. The CDU also favours tax cuts, though it seems in less of a hurry. Both parties are accused of making pie-in-the-sky promises, since they also insist that the budget deficit must be cut. The best cure for deficits is growth, retorts the FDP; that will not happen without tax cuts. As the campaign heats up, Ms Merkel will probably shy away from the FDP's radical ideas. Mr Westerwelle's task will be to change her mind if and when he joins her cabinet.

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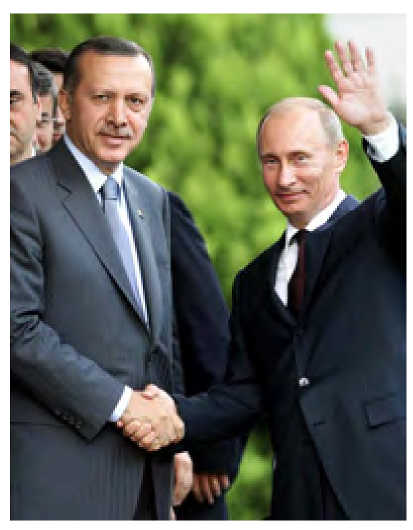
Turkey and Russia

Old rivals, new partners

Aug 13th 2009 | ANKARA
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An alliance of convenience that arouses some suspicion in the West

AFP



Friends or foes?

THROUGH the long Ottoman era, Turks and Russians fought many bloody wars. In modern times Turkey guarded NATO's southern flank against Soviet mischief. "The Russians are treacherous" is a popular Turkish adage. But one would hardly have guessed it as the two countries' prime ministers, Vladimir Putin and Recep Tayyip Erdogan, splashily signed a raft of agreements in a ceremony in Ankara on August 6th.

"Treacherous" was in fact the word some applied to the deal with Russia's Gazprom to use Turkish territorial waters in the Black Sea for a gas pipeline to Europe. The planned South Stream pipeline will bypass Ukraine, through which 80% of Russia's gas exports to Europe now flow. Russia has repeatedly turned off the taps in disputes with Ukraine, leaving millions of Europeans in the cold. To reduce dependence on Russia, the European Union has long promoted a pipeline to the Caspian, Nabucco, which Turkey also signed up for in July. So whose side is it on?

The answer is simple: Turkey's. Sitting at the crossroads of the energy-rich Middle East and the former Soviet Union, Turkey has unique leverage as a transit hub for gas. And it is unabashedly using the energy card to promote its membership of the EU. This requires co-operation with Russia. In exchange for backing South Stream, Turkey won Russian support for an oil pipeline from the Black Sea port of Samsun to the Ceyhan terminal on the Mediterranean. It is also said to have cajoled Russia into lowering the price for a nuclear-power station. Nabucco and South Stream are not rivals, they are complementary, insists Turkey's foreign minister, Ahmet Davutoglu.

The same might be said of Turkey and Russia themselves. With the end of the cold war their interests sometimes coincide. Both backed the war in Afghanistan but were viscerally opposed to America's invasion of Iraq. Turkey's image as America's poodle was erased in March 2003 when its parliament refused to let American troops cross Turkish soil to open a second front against Saddam Hussein.

A bigger test of Turkey's stance came in the Russia-Georgia war of August 2008. Turkey carefully implemented the Montreux Convention, which governs traffic through the Bosporus, so only a handful of American warships could enter the Black Sea. Neither Turkey nor Russia wants the Americans meddling in their back pond.

What do the Americans think? Ian Lesser, an analyst at the German Marshall Fund in Washington, argues that for now they are not fussed. "The [Obama] administration is far more sensitive to what Turkey does with Iran." Turkey's overtures to Russia are seen in the context of a new foreign policy that involves engaging with all its neighbours. Europe can hardly cast stones either, as it remains divided over Russia. Italy's prime minister, Silvio Berlusconi, was present in Ankara because ENI, an Italian energy company, is involved in the South Stream deal.

Russia is Turkey's biggest single trading partner and provides 68% of its gas. Turkish construction firms are active all over Russia. Millions of Russian tourists flock to Turkish resorts every year. Antalya, on the Mediterranean, is home to some 15,000 Russians, many of them women married to Turkish men. They have their own Russian-language newspaper and now want an Orthodox church. "Russian women educated Turkish men in love," says Ali Ozgenturk, who made "Balalayka", a film about Russian prostitutes in Turkey.

Mr Putin and Mr Erdogan get on well. Both are macho, sporty and prone to authoritarian instincts. Turkey is also one of the few countries with which today's Russia feels comfortable, a pole in its preferred multipolar system, in which big countries pursue independent policies. Turkey even appears to have

colluded with the Russian patriarch, Kirill, to limit the powers of the Greek Orthodox patriarch in Istanbul, Bartholomew I, usually seen as first among equals in the Orthodox hierarchy.

Yet mutual suspicions linger. Russia is unhappy with Turkey's indulgence of Chechens. (Tahir Buyukkorukcu, a Muslim preacher, speaks of the "Russian pig" when talking of Chechnya in his television show on the private Kon channel.) Russia has shut schools run by the Muslim fraternity of a Turkish imam, Fethullah Gulen.

For Turkey, Russia's refusal to label Kurdish rebels of the Kurdistan Workers' Party (PKK) as "terrorists" is a sore point. It is also wary of Russia's show of wanting to help Armenia and Azerbaijan make peace over Nagorno-Karabakh. Turkish officials say Russia wants to repair the damage to its image caused by its battering of Georgia. More likely, it wants to stop Turkey making peace with Armenia. Many believe that Russian scheming emboldened Azerbaijan to press Turkey into ditching plans to re-establish ties and reopen its border with Armenia. This is now patrolled by Russian soldiers, just as in the cold war.

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Zarema's end

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More brutal murders in lawless Chechnya


AP
Another funeral in Grozny

ZAREMA SADULAYEVA was not political. She did not investigate crimes committed by Russian and Chechen security men or write articles about them. She ran an independent charity that helped children traumatised, physically and emotionally, by two Chechen wars. Her organisation, Save the Generation, dealt with those who had lost limbs and parents.

On August 10th, in broad daylight, a group of armed men—some in military fatigues, others in civilian clothing—walked into her office and took away her and her husband, Alik Djabrailov (a former rebel). The men returned to pick up the pair's mobile phones and car. A few hours later, their bodies were found in the boot near Grozny, riddled with bullets. In their callousness and impunity the executions recalled the murder of Natalia Estemirova, a human-rights defender, a few weeks ago.

The two women worked across the street from each other and shared the belief that human life and dignity are more important than political expediency. It is not a belief apparently held by the Chechen or Russian authorities. Shortly after the murder of Ms Estemirova, Ramzan Kadyrov, Chechnya's president, told Radio Liberty that she had "no honour, dignity or conscience". His henchmen consider human-rights workers legitimate targets. Mr Kadyrov bears much responsibility for the climate of impunity and terror in Chechnya. With the silent blessing of Vladimir Putin, Russia's prime minister and his patron, Mr Kadyrov has created a totalitarian system in the province.

Mr Kadyrov has been expanding his personal power, acting more as a Kremlin ally than as a subject and state employee. If Moscow had the will to investigate the murders of human-rights defenders and to protect the few still working in the region, it could easily do it. But the murders remain unsolved and human-rights activists, lawyers and journalists continue to die (a journalist was killed in neighbouring Dagestan on August 11th).

An independent investigation in Chechnya would cause friction with Mr Kadyrov who is personally loyal to Mr Putin and whose means, in the Kremlin's eyes, justify the end of stabilising Chechnya. In fact, Russia's "victory" in the Chechen wars is deceptive. The entire north Caucasus remains a battleground, where people die daily. On August 12th armed rebels gunned down Ingushetia's construction minister. The Kremlin has not made Chechnya into an integral, law-abiding part of Russia. But it has moved Russia closer to Chechnya.

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Prospects for recovery

Mervyn's reality check

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The Bank of England foresees better times but remains wary

Illustration by David Simonds



FOR much of this summer, a recovery has shimmered on the horizon only to turn out to be a mirage. Now a genuine revival in Britain's swooning economy does look in sight. But it will bring scant comfort to anyone hoping for a swift return to business as usual.

That, in effect, was the unpalatable message delivered by the Bank of England on August 12th in its quarterly review of the economy. Presenting the findings of the *Inflation Report*, Mervyn King, the bank's governor, said it was likely that output had stabilised in the middle of this year. The bank was now more confident that the economy would pick up in the near future. But he gave warning that "recovery could be slow and protracted."

That recovery should be supported in the initial stages by a turnaround in the stock cycle, as producers start to meet demand by raising output rather than running down inventories. The fall in the pound will also help. Although sterling has bounced back quite a bit since its nadir at the end of last year, the trade-weighted index is still 20% lower than in the first half of 2007, before the financial crisis began. That should give British producers of tradable goods and services a competitive edge both at home and in foreign markets. More generally, the economy is being boosted by the extraordinary stimulus it is getting from monetary and fiscal policy.

But the recovery will be from a lower starting-point than the Bank of England envisaged in May, reflecting the dismal performance of the economy in the first half of the year (see chart 1). On the other hand, it will be somewhat stronger thanks to the bank's decision on August 6th to extend yet further its unorthodox policy of quantitative easing. It will purchase a further £50 billion ($83 billion) of assets with newly created money over the next three months, taking the total to £175 billion.

Moreover, the bank used the occasion to send a signal that it would be in no hurry to raise the base rate, which it brought down to an all-time low of 0.5% in March. The report presents projections for inflation on two different assumptions, the interest rates expected by the markets and the base rate being left

unchanged. By comparing the two forecasts it is possible to infer how realistic the bank judges market expectations to be.



The City had been expecting the base rate to rise next year, to reach just over 2% by the end of 2010 and to carry on rising in 2011. On this basis, consumer-price inflation would be below the 2% target in two years' time—the period it normally takes for monetary policy to have its full effect on prices (see chart 2). If instead the base rate were held at 0.5%, inflation would be hitting the target in mid-2011. In practice the bank is highly unlikely to keep interest rates on hold in this way, but it does not have to raise them as quickly as the markets had been expecting.

One worry about the programme of quantitative easing is that it will stoke inflation. The bank's inflation forecasts suggest that such a concern is unwarranted. The recession has been so severe that a big gap has opened up between the productive capacity of the economy and actual output. While this persists it will constrain inflationary pressures—and given the gap's size, it is likely to last a long time, even with a healthy recovery.



As if to underline the point, official figures on the labour market published on the same day as the bank's report showed earnings (excluding bonuses) rising by only 2.5% in the year to the second quarter, compared with 3.8% a year earlier. That is unsurprising given the damage wreaked by the recession. There was a record fall in employment of 271,000 between the first and second quarters of 2009. And unemployment rose to 7.8% of the labour force in the second quarter, up from 5.4% a year earlier. That brought the total number of jobless up to 2.4m, the highest since 1995. John Hawksworth, an economist at PWC, an accountancy firm, says unemployment is on course to reach 3m next spring.

Mr King may be rather more confident about an upswing in the near term, but he continues to worry about whether it will prove sustainable further ahead. Banks still have much work to do to repair their ravaged balance-sheets, which will limit their ability to lend. Meanwhile, a fragile banking system remains vulnerable to further shocks. The Bank of England's report identifies "persistent weakness in bank lending" as a downside risk to spending over the next three years.

So much still to worry about

Households must also sort out their finances after a decade of overborrowing. They will need to save more both to make up for falls in wealth and to keep more aside in case they become unemployed. Higher saving together with subdued earnings "is likely to result in relatively weak household spending growth", says the bank.

There are other risks. The bank is expecting net trade to bolster the recovery, as exporters press home their gains in competitiveness once foreign markets recover. But, as the report points out, "the outlook for global demand is highly uncertain," not least since other countries are facing the same difficulties. A world recovery may also prove fragile if it prompts big commodity price rises.

The Bank of England's overall prognosis may appear gloomy; but it is realistic. The recession has taken a terrible toll on output, which has fallen by 5.7% since the start of 2008. The genesis of the downturn—a financial crisis that came close to toppling Britain's banking system—is one that augurs ill for a robust recovery. Moreover, the emergency monetary and fiscal treatment must eventually be withdrawn, which will create moments of peril ahead. With an election due by the middle of next year, Labour and the

Conservatives will be fighting over a miserable inheritance.

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The politics of defence

The thinning red line

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Military spending cuts are likely under the next government, whoever forms it

Reuters

An obscure future for the armed forces

BOTH Bob Ainsworth, the defence secretary, and Liam Fox, his Conservative opposite number, have pledged to hold a strategic review of defence after the next election. When the last one was carried out, in 1998, taxes were cascading into the Treasury; they are now drying up. The armed forces, now losing troops frequently in Afghanistan, were yet to be tested in Kosovo and Sierra Leone, let alone by the long wars that followed farther east.

Shaping a defence policy amid austerity will be particularly tough for Labour. Its relations with the forces have suffered as the military has been given bigger burdens without matching resources. A spell in opposition could revive the historical split between Labour's hawks and doves. A party with a diminished vision for Britain's role in the world, and the military spending needed to fulfil it, could emerge.

The old Labour right, with its no-nonsense attitude to national security, once harboured big beasts such as Ernest Bevin, the post-war foreign secretary who took Britain into NATO, and George (now Lord) Robertson, who oversaw the last defence review. But they are rare now. Younger "Blairite" MPs share the former prime minister's ardour for domestic reform and, at a push, Europe, but not his fighting zeal.

Yet neither the Tories' old affinity with the forces, nor the hawkishness of Mr Fox and George Osborne, the shadow chancellor, justify optimism among defence chiefs about a putative Conservative government. David Cameron, the Tory leader, has not exempted defence spending from the coming austerity push. The most recent Tory government shrank it, even before the Cold War ended. And the party may only get away with cutting overall spending if it takes the axe to traditional Tory causes as well as softer targets.

Not even the Liberal Democrats, Westminster's peaceniks, support nuclear disarmament. Under the Tories, the deterrent is likely to continue to take the form of the Trident submarine fleet. But savings could be found, most radically by operating three rather than four vessels. Pay, which in recent years has risen more than the Ministry of Defence had anticipated, may also be targeted. Malcolm Chalmers of the Royal United Services Institute, a think-tank, says even a modest cut to planned pay could yield significant savings. But stinginess towards soldiers is politically risky, as recent rows over compensation to wounded servicemen have shown.

Thanks to the ministry's reputation for waste, cuts in procurement could be comparatively uncontroversial. On August 6th ministers were forced to deny that an official report exposing profligacy in defence procurement, which was due to be published last month, had been suppressed. But identifying projects to scrap or shrink is tough. Delaying purchases often generates long-term costs. Some projects, such as the two new aircraft carriers and the third tranche of the Eurofighter Typhoon aircraft, may be too far

advanced to scale down much.

If there is hope for the top brass, it is that Britain’s defence strategy will in the end be shaped by its international ambitions. Judging by a recent speech by William Hague, the shadow foreign secretary, or the admittedly little that is known of Mr Cameron’s foreign-policy instincts, a drastic curtailing of these under the Tories is unlikely. A repeat of the scale and frequency of Mr Blair’s wars seems fanciful, but so does the prospect of Britain guarding its own turf and wishing the world away.

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Bankers' bonuses

Watered down

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A new code on rewarding bankers will not restrict payouts

NOBODY trembled when the Financial Services Authority (FSA), Britain's financial watchdog, unveiled a new remuneration code for banks on August 12th. Rather than prescribing how big banks should mend their executives' pay, it merely suggested some remedies. At issue are the perverse incentives which led some bankers to pitch their banks, and the entire financial system, into peril. Those who suffered were not usually these overpaid employees but shareholders and taxpayers—and customers, who may have been ripped off along the way.

Anyone hoping for a radical change will be disappointed—though the City will be relieved. The FSA's initial draft in March contained threats to limit the share of bonuses that can be taken in cash, forcing at least two-thirds of the payout to be deferred and depend on future performance. Those threats have turned into "recommendations" that can be ducked, provided a bank can explain its behaviour. The FSA's only real sanction will be to require a bank to put up more capital if its remuneration policy is judged over-risky. But how would the riskiness be calculated by anyone outside the bank?

Peter Montagnon, investment-affairs director at the Association of British Insurers, which broadly applauds the new code, agrees that the calculation is a sticking-point. But "perhaps the threat of a higher capital requirement is enough," he says.

Nor did the FSA seem exercised by the news earlier this month that Barclays, a rapidly expanding bank, had agreed to pay a few new recruits multi-year guaranteed bonuses. The practice seems to be alive and well among banks trying to steal what they regard as top talent from each other.

Hector Sants, the FSA's chief executive, maintained recently that the size of individual payments was a question not for the regulator but "for politicians and society as a whole". Few in Westminster appear to have any appetite for it, though in France it is a different story. There, the government has ruled that bonuses, limited to a one-year guarantee, must be paid out of profits, not revenues (see article).

The Conservative Party, which is likely to form the government after the next general election, to be held by June at the latest, is also reluctant to be prescriptive. "We don't want a cap on pay, apart from a limit on cash bonuses paid to those in state-controlled banks," says an adviser to George Osborne, the shadow chancellor. "But we don't want business as usual either." The party would like to turn the FSA into a consumer-protection agency and give financial supervision to the Bank of England, which would be less inclined to kowtow to bankers, he says.

At the heart of the general reluctance to be radical is a fear that unilateral measures might drive big banks away from London, putting its dominant financial position at risk. That is the main reason why the FSA's code has been watered down, as its preamble admits. It will apply only to around 26 of the biggest banking operations based in the capital. And it looks unlikely now to be any tougher than standards being developed by the Basel Committee on Banking Supervision, a rich-country forum, and by the European Union.

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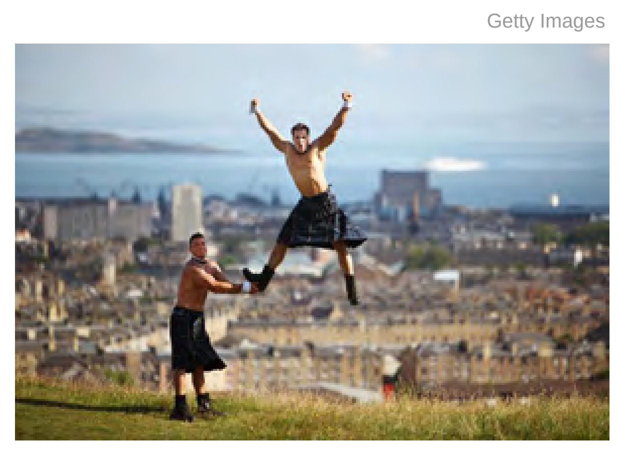
Scotland's capital and recession

Party time

Aug 13th 2009 | EDINBURGH
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Looking for an upside to the downturn

Getty Images



On the up, at least for now

PICKING past rotting rubbish left after an on-off strike by refuse collectors, and wending their way around streets blocked by seemingly endless roadworks for a new tramline, visitors to this year's Edinburgh International Festival might well think the city is in serious trouble. With its once-mighty banks, RBS and HBOS, the heart of the Scottish capital's financial industry, brought low by reckless profligacy, the problems look deep.

Indeed, before the credit crunch 11% of Edinburgh's jobs were in financial services and about half were in these two big banks. Over the past year the number claiming unemployment benefit has risen by 75% (though, at 3.2%, the city's claimant rate is still below the national average).

Yet the discerning visitor may also notice something else. Streets and restaurants are jam-packed; pubs and clubs are buzzing. Festival and Fringe ticket sales are way up on last year (see article), only partly because the number of Scots drinking in the arts at home instead of wine in the Mediterranean has shot up.

Fuelled by the weak pound, which has made Britain much cheaper for Europeans than two years ago, Edinburgh has been enjoying a tourist boom. The number of passengers passing through its airport has risen each month since March, and by 5.6% in July, the only British airport to record such growth. BAA, its owner, reckons that since domestic British air-passenger numbers have dropped by about 5%, the increase comes entirely from European sightseers taking advantage of 20 new international routes added since January, mainly by budget airlines.

The national recession has had another surprising effect: a big rise in the number of foreign firms investing in Edinburgh. Thirteen have come in during the first half of 2009, compared with 12 in the whole of 2008. Greg Ward, of the council's economic development unit, thinks investors had been put off by the city's high employment rate, which stood at just over 80% of the working-age population in 2008. They feared having to pay too much to recruit the people they needed. Rising unemployment, in particular among the highly skilled, has eased those worries.

Some established financial firms are also expanding. Tesco Personal Finance has announced plans to increase staff at its Edinburgh headquarters from 250 to 450 by the end of the year. Virgin Money also announced plans to grow. Even property prices have fallen by only half as much as in comparable British cities. All in all, civic leaders feel justified in boasting that Edinburgh is weathering the recession well.

This satisfaction may not last. The slimming-down of RBS and the cost-cutting integration of the

operations of Lloyds and HBOS have yet to take their full toll. Of their combined pre-crisis workforce of about 18,000, only around 500 have lost their jobs so far. More will no doubt follow.

If the economy does recover as fast as the government hopes, the currency advantage now enjoyed by Europeans may disappear and the travellers with it. And this year's stay-at-home holiday-making Scots (78% of fringe credit-card ticket sales have an Edinburgh postcode this year, up from 60% last year) may revert to sun-seeking. Meanwhile, the city is partying.

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Edinburgh festivals

Fringe-onomics

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From The Economist print edition

The macro and micro of an impromptu festival

Eyevine



On the prowl for an audience

ANXIOUS father shuts his eyes. Forget the £4,000 it has cost to bring his teenage son's play to Edinburgh: as the house lights go down, please let there be no humiliation.

Performers of all kinds, from schoolboy writer-directors to stars with household names, are drawn to the Edinburgh Festival Fringe like moths to a giant searchlight. More than 260 venues, from big theatres to dim vaults, even moving buses, provide the platform for more than 2,000 shows over 25 days in August.

The Fringe began as a foil to the snootier Edinburgh International Festival of music and theatre. Now, some 60 years on, it dwarfs the original, generating £75m of the £200m that the city's twelve main festivals bring in each year. (That includes not just tickets, but accommodation, food and drink for the estimated 4m visitors they attract.) All the signs are that this will be a record year for the Fringe, with advance ticket sales 20% up on 2007.

Unlike the curated and subsidised International Festival, the Fringe is open to anyone with a little money and plenty of passion. The Edinburgh Festival Fringe Society, incorporated in 1969, exercises no quality control, but just prints the programmes, runs the box office and provides support, such as rehearsal space.

Quality control, such as it is, is exercised at the bigger venues. At the Assembly Rooms, the Pleasance and the Underbelly, for example, entrepreneurs try to ensure that most of their big spaces are packed, by using big names and tested shows, a heady mix of two-fifths comedy, two-fifths theatre, and the rest music and dance. Each turns over several million pounds in ticket and drink sales.

But the Fringe is also about those hopefuls—stand-up comics, actors, writers and musicians—to be seen canvassing on the cobbled Royal Mile below the castle. They compete to bring their show to the attention of a reviewer, or even one of the 1,200 talent scouts rumoured to be hunting for the next big thing.

Though the Fringe has an international reputation, around two-thirds of its audiences comes from the Edinburgh region, a figure that surprises most visitors. "The locals see it as their festival, which is a good thing," says Faith Liddell, director of Festivals Edinburgh, an umbrella body which seeks to co-ordinate the festivals where possible. "Thundering Hooves", a 2006 review of Edinburgh's offering, gave warning of what could happen if those responsible failed to provide efficient and attractive infrastructure. Last year the Fringe Society's online ticketing-system crashed, denting sales and the festival's reputation.

"It showed us how fragile the whole thing is," says Kath Mainland, the Society's post-fiasco chief executive. She has her eyes set on 2012 when the August festivals overlap with the Olympic Games in London. Will it be a clash or a fantastic opportunity to cross-sell? By then the intrepid teenage playwright will be nearly 20 and, if not too dispirited by his "mixed" review in the *Scotsman*, may return with something sensational.

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Swine flu

Summer lull

Aug 13th 2009
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The latest confusion over the disease of the moment

WEB-SAVVY Britons who feel shivery and achey can now go online and spend a few minutes answering questions about their symptoms and general health. (Old-fashioned types can call a helpline, and speak to a human.) If a diagnosis of swine flu seems likely, they will be given a number and the address of an antiviral collection point. Their "flu friends"—all Britons are supposed to have arranged one by now—can then pick up their medicines. Only pregnant women, and other vulnerable groups, should bother their doctors.

Alas, this elaborate new system has provoked fresh concerns. Employers fret that skivers can easily get time off work by faking symptoms to a computer screen, or to a hastily trained voice on the other end of a phone line. More seriously, doctors warn that other ailments, from measles to meningitis, may be misdiagnosed, with potentially tragic consequences.

The medicine being doled out, Tamiflu, is itself a worry, for evolving reasons. When swine flu first hit the news in the spring, ministers faced questions about whether Britain had stockpiled enough of it. But now they are under attack for a different reason. A review of studies of the use of antivirals to treat ordinary seasonal flu, published by the *British Medical Journal* on August 10th, suggested that administering them to children reduced the duration of the disease by just 12-36 hours. It also confirmed anecdotal reports of side-effects. The researchers found little to indicate that the benefits of giving them to children for mild cases of swine flu would outweigh the risks. Commentators have switched from asking whether Britain has enough Tamiflu to whether it is prescribing it too freely.

The move from GP consultations to the new, multimedia pandemic service may have helped to slow the disease's spread. The week after the switchover, the number of fresh cases fell significantly, with a best estimate of 30,000 new cases, down by two-thirds from the previous week. Nor does the disease seem to be becoming more serious, or resistant to antiviral drugs. Though there have been 49 deaths "related to swine flu" in Britain so far, officials point out that such a verdict does not mean the disease delivered the killing blow. Most probably, the lull is due to the summer holidays. The real test of the new strategy will come in the autumn, when schools reopen.

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Bagehot

Love in the time of swine flu

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From The Economist print edition

Britain's long, hot-and-cold summer of uncertainty

Illustration by Steve O'Brien



SUMMERS often have a flavour. There have been summers of love and revolution and, in Britain, of urban riots and battles between mods and rockers. The country's most memorable summers include the glorious one of 1940, when the Royal Air Force repelled the Luftwaffe, the sweltering one of 1976, and, for their sporting triumphs, 1966 (football) and 1981 (cricket). The summer of 2005 will go down as a time of terrorism. The current one has a distinctive atmosphere too. It is a summer of apprehension, of uncertainties in various aspects of public life that have seemed strangely to reinforce one another.

One symptom of the mood is the muddle over swine flu. When the disease first appeared in April, it was big news. Then the media's attention wandered—just as the virus took off. As summer arrived, the serious scaremongering started. There was talk of mass school closures; travellers on the Tube began to reach for the SARS-style face masks. Parents pondered dispatching their children to "swine flu parties", to contract the illness before it mutated. There have been worries over whether the recommended medicine is safe. Yet now the rate of new infections seems to be slowing (the statistics are so unreliable that it is hard to say for sure), and the plague seems less threatening.

The same sort of ambiguity—about whether the woe is just beginning or petering out, will be mercifully brief or utterly ruinous—clouds the economic news too. Take the banks. Some are back in profit and shelling out controversial bonuses; some have called the bottom of the spiral of bad debts and write-downs that devastated them. But others are struggling. And despite the government's huge stake in the banking sector, businesses, especially small ones, complain that credit is still desperately scarce.

The blurry banking picture reflects the contradictory outlook for the quantitatively eased economy. There have been encouraging summer figures on house prices, the rebounding service sector, the car industry, the stockmarket and consumer confidence. But there have also been demoralising numbers: unemployment is still rising fast, insolvencies are commonplace. The recession is said by some to be over, but it has been deeper than was once anticipated, and the economy may yet dip again. The Bank of England shares the widespread doubt and trepidation about its prospects. Meanwhile the government's fiscal deficit is prodigious and its debt vaulting, raising the fundamental issue of what kind of state Britain will be able to afford after the economy has indeed recovered.

One facet of that awkward problem is whether Britain will, in future, be able to fight the sort of war in

which it is currently embroiled in Afghanistan. Over the summer, as soldiers have died in Helmand, arguments have raged at home about the treatment and equipment they receive. For the first time the political consensus about Britain's involvement in the conflict has seemed strained. Beneath those wrangles lies a broader anxiety over Britain's place in the world: about whether it should continue to pursue a global military role, or cast off such aspirations as post-imperial hubris and reconcile itself to a humbler status.

Harmania and Megalo-Mandelson

Behind all these quandaries, of course, lies the summer's basic political mystery. By this time next year, who will have responsibility for resolving them?

The government has staged its usual summer pantomime in recent weeks, the one in which the prime minister pretends to take a holiday, leaving others to mind the Downing Street shop. When Tony Blair jetted off to a paradisal beach or palazzo, the cameo mostly fell to John Prescott, his comic sidekick. Under Gordon Brown, first Harriet Harman, the leader of the Commons, and now Lord Mandelson, the formidable First Secretary, have filled in. Both have supplied the necessary entertainment, Ms Harman with some opportunistic grandstanding, Lord Mandelson by starting his stint while still in Corfu, then reviving his feud with George Osborne, whom he bumped into on the same island last year (with uncomfortable results for the shadow chancellor).

The real ambiguity, however, is not over who is running the country now, but who will do so after the impending general election. David Cameron, the leader of the Conservatives, is much the likeliest candidate. But the prospect of a Tory victory carries further unknowns. How, precisely, would the Tories rectify the fiscal position, as they frequently but vaguely pledge to? (Mr Osborne was at it again this week, making a provocative but sketchy speech on the savings to be made through public-service reform.) How would it feel, after a gap of 13 years, to have a Conservative government? What sort of society would it fashion?

The annual round of party conferences, beginning next month, will in effect mark the launch of a long, long election campaign. The Tories will have to supply a more comprehensive prospectus than they have so far. But the summer months, as they generally are, have been a hiatus in serious politics, before the brutal end-game. For now the country knows the questions but has heard few answers. It is more uneasy and bemused about the coming political showdown than eager and excited.

In fact, even the customary vagaries of the British summer have this year been peculiarly disorienting. First, England's cricketers vanquished the visiting Australians; not long afterwards the Australians inflicted a humiliating rout on their prematurely lionised hosts. The weather, so balmy in June, reverted to rainy type in July, confounding predictions of a prolonged scorcher, leaving the meteorologists red-faced and the skin of stay-at-home Britons pallid. The oscillating sunshine and drizzle have epitomised the mood in the country they fall on. For Britain, this has been a summer of rumbling doubt and confusion.

Economist.com/blogs/bagehot

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Correction: Teaching in Britain

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In "Those who can", published on August 1st, we said that nearly a tenth of Oxford's class of 2009 will be participating in the Teach First programme this autumn. In fact, nearly a tenth of those who will be Teaching First this autumn are Oxford graduates. Sorry.

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The Geneva conventions at 60

Unleashing the laws of war

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From The Economist print edition

The chasm is still too wide between noble Swiss ideas and the hard reality of locations where war is hell

AP



Bosnia, where treaties didn't help

WALK the calm, well-heeled streets of Geneva and there seems little to connect this metropolis in neutral Switzerland with the genocidal slaughter in Rwanda and the rape camps of Bosnia in the 1990s, or the appalling violence lately inflicted on civilians caught up in fighting in Darfur, Chad or eastern Congo. Yet decisions taken in Geneva do have an effect, both legal and humanitarian, on people in benighted places—and the world would be much happier if the effect was far greater.

The city is the UN's humanitarian hub, headquarters to both its refugee and human-rights agencies. More memorably, though, it lends its name to a clutch of conventions, adopted six decades ago this month, initially with the horrors of two world wars in mind. Those agreements still form a bedrock for the laws of war and the protection of non-combatants.

Yet in a year that has already seen bitter fighting in Gaza and Sri Lanka, and a still mounting civilian toll in an eight-year-old battle against the Taliban in Afghanistan, some inevitably question whether the Geneva conventions and their later protocols are really suited to today's conflicts. The number of wars between states, where regular, uniformed armies square off against each other, has fallen sharply. This century it has mostly been conflicts within countries that have claimed headlines, with insurgents and rebels, sometimes with foreign backing, battling each other as well as their own government.

Do the old rules really apply in such conflicts? And if they still do, how can they be enforced more effectively, since all the evidence suggests they are not only not honoured but dishonoured in the breach? Can they be stretched to cover new threats, such as international terrorism and piracy?

To the chagrin of those who would banish war itself, neither the four Geneva conventions of 1949—covering the treatment of the wounded on land and at sea, of prisoners-of-war and of civilians caught up in conflict—nor the couple of extra protocols added in 1977, spelling out in more detail the protection afforded to civilians, seek to outlaw conflict (see table below). Nor do they presume (although they do more for the innocent than the earlier Hague conventions, which concentrated chiefly on outlawing some weapons of warfare) that civilians in a war zone always can be or even should be spared.

Their aim is more modest. It was spelled out under prodding from the Geneva-based International Committee of the Red Cross (ICRC), itself set up by a Swiss businessman appalled at the carnage of the Battle of Solferino in 1859, a European punch-up between forces from Austria, France and Italy. The idea is to inject some basic humanity into the conduct of all sides in a conflict.

Limits to inhumanity

Conventions on the laws of war

Year	Convention	Description
1899	**Hague Convention**	focused on conduct of war; banned use of certain types of new technology in war, including hollow-point bullets and shelling with asphyxiating gases
1907	**Hague Convention**	increased focus on naval warfare
1925	**Geneva Protocol**	not negotiated in The Hague but considered an addition to the convention; permanently banned all chemical and biological warfare; has since been augmented by the Biological Weapons Convention (1972) and the Chemical Weapons Convention (1993), which outlaw production and stockpiling too
1949	**1st Geneva Convention**	protects wounded and sick soldiers on land during war; follows conventions adopted in 1864, 1906 and 1929
	2nd Geneva Convention	protects wounded, sick and shipwrecked military personnel at sea during war
	3rd Geneva Convention	applies to prisoners-of-war
	4th Geneva Convention	protects civilians, including in occupied territory
	Common article 3	common to all four conventions; obliges the humane treatment of all persons in enemy hands, with no derogation permitted
1977	**Additional Protocol I**	strengthens protection of victims of international armed conflicts
	Additional Protocol II	strengthens protection of victims of non-international armed conflicts; first international treaty devoted exclusively to such conflicts
2005	**Additional Protocol III**	Red Crystal emblem adopted, which has the same international status as the Red Cross and Red Crescent emblems

Sources: ICRC; *The Economist*

Indeed, the ICRC points out that "common article 3" of the 1949 conventions requires the humane treatment of *any* person in enemy hands; then and even earlier, it was clear that such an obligation applied to parties to wars fought within a country's borders, not just across them. The second of the two 1977 protocols, meanwhile, applies specifically to non-international conflicts and cements and extends such obligations in treaty law.

So if the rules are clear, why can't civilians find better protection in conflict zones? One problem is that, although the four 1949 conventions have been signed by all countries, support for the tougher 1977 ones still lags. Among the missing in action are both India and Pakistan, who not only square off against each other from time to time but also face violent insurgencies inside their borders. Other absentees include Afghanistan, Iran, Israel, Malaysia, Myanmar—and the United States. Others, it has to be said, have signed and yet blatantly ignore the rules.

How can such countries and individuals be brought to book? Upholding the rules is bound to be hardest where people simply do not know about the sorts of protection that the conventions and protocols are supposed to afford. A survey commissioned by the ICRC to coincide with the 60th anniversary of the 1949 conventions found that knowledge of them was patchy, even in places that had recently seen conflict. Nearly 60% of those asked had not heard of the accords. Of those who had, 44% thought they did little or nothing to limit the suffering of civilians in war zones.

The ICRC works hard both to disseminate information about the conventions and to get governments and others to teach the rules to their armed forces. When conflicts erupt, it seeks to get all parties to commit to observing the rules by way of special agreements. It has also drawn up more detailed guidelines, though these are only advisory, to help military commanders distinguish more clearly between who is a civilian, and therefore to be protected where possible, and who is not and thus potentially a legitimate target. Yet, as even some of the best-willed practitioners point out, getting from principle to practice will always be hard: each situation is different and even the most carefully written rules will seldom be an exact fit.

When impunity persists

In any case, better than new rules would be more effective enforcement of those that already exist. For a

while, after the horrors of the 1990s in Europe and Africa, there was hope that ending impunity for the worst offenders might curb the worst excesses in conflicts. Yet here the prospects seem again to be turning bleak.

Take the issue of rape and other sexual violence in wartime. Although implicitly covered by earlier prohibitions on inhumane treatment, the 1977 Geneva protocols explicitly outlawed rape as a weapon of war. Building on all this, the international tribunal for Rwanda, set up to bring the perpetrators of genocide to justice, was the first to prosecute wide-scale sexual violence as attempted genocide. A UN-backed tribunal for former Yugoslavia took harrowing testimony from Bosnia's many victims and convicted some of their tormentors. The court for Sierra Leone extended the arm of law to cover forced marriage, a feature of other conflicts too, whereby young women are given as "wives" to rebel fighters. Likewise the International Criminal Court (ICC), the world's first permanent war-crimes court, established at The Hague in 2002, included sexual violence in its early indictments.

Yet the prospect of being held to account has so far proved less of a deterrent than was hoped. If anything the use of rape as a weapon of war is on the increase.

Although Islam condemns rape, it has been used by Arab *janjaweed* militias against black fellow Muslims in Sudan's Darfur region on a scale that has been likened to genocide. The UN secretary-general, Ban Ki-moon, recently said he was "haunted" by the scale and depravity of sexual violence in places like Congo, committed by both rebel and government forces. Some 16,000 new cases of sexual violence, 65% of them involving children, were registered in Congo in 2008, said Susan Rice, America's UN ambassador, quoting figures from the UN Population Fund in a recent Security Council debate. Experience in the field suggests that, as a rule of thumb in these conflict zones, the number of actual cases is probably ten to 20 times greater than the number reported.

AP

Bosnia, where treaties didn't help

In a report to the council this month, Mr Ban's list of conflicts where rape has been widespread ran from Chad and the Central African Republic to Afghanistan under the Taliban, Myanmar and Nepal. But it is not just the numbers that are depressing.

Some of the countries that signed up to the ICC appear to be experiencing buyers' remorse. The African Union (AU) was the first regional organisation to talk of moving from non-interference (the claim that governments can do what they like within their own borders) to non-indifference to such crimes. African governments make up about a third of those that have ratified the ICC's Rome statutes, which oblige them to help the court track down those it has charged. Yet a recent AU summit voted to end co-operation with the court over its indictment of Sudan's president, Omar al-Bashir, for war crimes and crimes against humanity in Darfur (a charge of genocide was dropped until ICC pre-trial judges can be sure the evidence warrants it).

The AU vote has been deplored by a number of African governments and by a long list of African human-rights groups. Critics of the court argue it is biased: all four cases it has taken on so far are from Africa. But of the four, three were referred by the governments themselves (Uganda, Chad and the Central African Republic), and the fourth, Sudan, was referred by the Security Council.

The backlash against the court is unlikely to help the battle to end impunity. Nor will the antics of the 47-member UN Human Rights Council (an inter-governmental body also based in Geneva that is nonetheless separate from the office headed by the UN's commissioner for human rights). Earlier this year a majority on the council gave Sri Lanka a pat on the back despite appalling loss of life among civilians caught up in the defeat of the Tamil Tigers. Not long before, it had lambasted Israel for its war in Gaza, mandating a fact-finding commission to look into what it said were Israel's "war crimes", while saying nothing at all about the actions of Hamas. The mission, led by Richard Goldstone, a prominent international lawyer, who reportedly sees his mandate in a less one-sided fashion, is due to report in September.

Meanwhile asking the ICC to take on other international crimes, such as terrorism and piracy, looks a non-starter. There is no agreed definition of terrorism beyond the "we know it when we see it" rule that lets one man's terrorist off the hook as another's freedom-fighter. In any case, the ICC has yet to pin down the fourth crime mentioned in its statute alongside war crimes, crimes against humanity and genocide: the crime of "aggression".

At a review conference next year, some will press for this charge to be added to the court's detailed sheet of punishable crimes. That would be premature. Informal discussions among the signatories to the court and some interested outsiders have produced tentative agreement on a definition of aggression. China and Russia have joined the talks, though they are not signatories. The United States, another non-signer, has held aloof, though the Obama administration could yet decide to take part. Trickiest of all, however, will be to figure out a way for the court to finger an alleged culprit without treading on the prerogatives of the UN Security Council, which is supposed to decide on all matters of war and peace.

Eventually a mechanism may be agreed that involves the council. America, China and Russia are unlikely to join the court until that happens and even then may not. The Geneva conventions are taking a battering, and the victims of war are still getting short shrift. But count on the big powers to hold their own ground.

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America loses its landlines

Cutting the cord

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Ever greater numbers of Americans are disconnecting their home telephones, with momentous consequences

Alamy



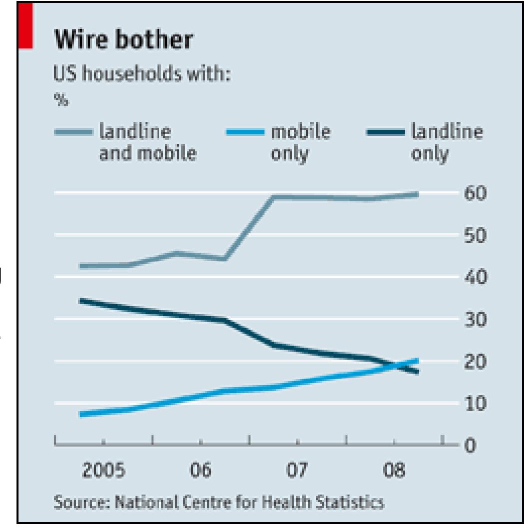
MUCH has been made of the precipitous decline of America's newspapers. According to one much-cited calculation, the country's last printed newspaper will land on a doorstep sometime in the first quarter of 2043. That is a positively healthy outlook, however, compared with another staple of American life: the home telephone. Telecoms operators are seeing customers abandon landlines at a rate of 700,000 per month. Some analysts now estimate that 25% of households in America rely entirely on mobile phones (or cellphones, as Americans call them)—a share that could double within the next three years. If the decline of the landline continues at its current rate, the last cord will be cut sometime in 2025.

The impact of this trend will be greater than most people realise. It will make life increasingly difficult for telecoms firms, naturally. But it will also hurt all business that require landlines, as bills rise and business models are disrupted. No less seriously, the withering fixed-line network threatens the work of the emergency services, such as the police and fire brigade.

The decline in landline use, which has been under way for several years, has picked up speed in recent months. In the first half of 2005 only 7.3% of households were mobile-only, according to America's Centres for Disease Control and Prevention (CDC), which collects such data because it uses landlines for health surveys. By the end of last year the proportion had reached 20.2%—increasing by 2.7 percentage points in the second half of last year alone, the biggest-ever increase (see chart).

The recession has accelerated cord-cutting, explains Stéphane Téral, an analyst at Infonetics Research, since people want to save money and are readier to sacrifice their landlines than their mobiles. But the problem is particularly acute in America because of the vastness of the country, which makes fixed-line networks expensive to run or improve. That, along with upheaval in the telecoms industry in recent years, has made internet access over landlines in America annoyingly slow, even in the cities, leaving landlines much more dispensable than they are in Europe.

All this would not matter much, were it not for the fact that many businesses depend on landlines. First to suffer are telemarketers, though they cannot expect much sympathy. Mobile numbers are harder to get hold of, and in most cases it is also against the law for telemarketers to call them (although many still do), since mobile users in America are charged for receiving calls as well as making them.



The growing ranks of people who only use mobiles are also causing trouble for polling firms. Most pollsters ignored them until early last year. But then the Pew Research Centre for the People and the Press, an outfit that studies public opinion, demonstrated that by shunning "cellphone- onlys" (CPOs), pollsters would understate Barack Obama's margin over John McCain in the presidential election by two to three percentage points.

CPOs are twice as expensive to reach, not least because outfits like Pew offer payments to those surveyed by mobile phone to compensate for the associated call charges. Worse, pollsters do not know much about them. They are typically in their early 30s, earn less than $50,000 annually, are unmarried and move more often than the norm. But even controlling for these factors, they still had distinctive voting preferences, says Brian Schaffner, a professor at the University of Massachusetts Amherst. According to his calculations, 49% of landline respondents leant towards Mr Obama in June 2008, but the figure was 65% among CPOs. Perhaps, he speculates, CPOs are "more willing to venture into something new".

And then there are the telecoms operators themselves. Surprisingly, the industry's heavyweights do not seem to be too worried about losing landlines, whether to mobile operators or cable companies, which now have 20% of the landline market. Their spokesmen argue that they have seen the trend coming and have invested in new businesses. Verizon, for instance, serves nearly 20m landline customers in America's north-east, but is also the country's biggest mobile operator with 87.7m subscribers and is investing billions in a new fibre-optic network which reaches 2.5m homes. Verizon has sold bits of its landline businesses in three states and is negotiating to do the same elsewhere.

Nonetheless Verizon and AT&T, its main competitor, are still mostly "wireline", says Craig Moffett, an analyst with Bernstein Research. According to his calculations, both firms' landline businesses generate more than 50% of revenues, and an even higher share of costs. The two firms and Qwest, America's third-biggest landline operator, have already shed thousands of jobs and announced further lay-offs to cut costs. But the accelerating loss of landlines will put increasing pressure on profit margins, argues Mr Moffett, as the high fixed cost of running the network is spread over an ever smaller number of customers. It is also likely to lead to higher bills for captive customers such as businesses with switchboards, which cannot do away with their landlines so easily.

Even if Verizon and AT&T can overcome their "wireline problem", says Mr Moffett, it will not go away. Most telecoms operators do not have a mobile business to fall back on. Fairpoint, a firm which took over some of Verizon's landline business, is struggling. Hawaiian Telcom filed for bankruptcy in December, not least because it was losing landline customers at a rapid clip. Such a fate raises the question of what will happen to the industry's huge unfunded pension liabilities. Taken together, the future obligations of AT&T and Verizon are as big as those of General Motors before its recent bankruptcy.

Regulators will not just have to decide whether to subsidise or bail out landline firms. They will also have to make sure that public goods delivered via the old telephone network continue to be provided. The call-tracing software used by firefighters, ambulance services and many other "first responders" only works on landlines. And the government-imposed cross-subsidy scheme to ensure that anyone who wants a telephone line can have one is primarily geared towards landlines. As the number of lines goes down, the subsidy required to provide lines to remote locations and poor customers will have to rise.

The danger, says Mr Moffett, is that regulators will introduce new taxes on wireless and broadband services. Revenues from new services would then be used to keep an obsolete infrastructure alive—a recipe for lower growth. At that point, he says, the "wireline problem" really will be everyone's problem.

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Economist.com BUSINESS

Boeing and Airbus argue about subsidies

Trading blows

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The two big aircraft-makers battle it out at the World Trade Organisation

AFP



Who paid for it?

NOT a lot has gone right for Boeing recently. After declaring to the world at the Paris air show in June that its chronically delayed 787 Dreamliner would take to the air before the month was out, executives were forced to announce an indefinite postponement of the high-tech aircraft's first flight only days later because of a problem with the wing mounting. The company also seems to have been hit harder by cash-strapped airlines cancelling orders than its main rival, Airbus. But Boeing is anticipating a triumph in the next few weeks when the World Trade Organisation (WTO) comes to a preliminary decision on a complaint made by America nearly five years ago about subsidies given to Airbus by European governments.

In 2004 at the urging of Harry Stonecipher, Boeing's boss at the time, America terminated a 1992 agreement with the European Union regulating government support for the commercial-aircraft industry and initiated a WTO dispute-settlement procedure. The agreement had capped European launch aid for new airliners at 33% of all development costs on condition that the money was repaid at an interest rate that at least covered the cost of the governments' own borrowing. For their part, the Americans were allowed to continue with indirect federal and state support for their aircraft industry as long as the payments did not exceed 3% of the industry's sales. Much of the subsidy received by Boeing comes in the form of research contracts for its military arm, the results of which can then be applied to its civil aircraft without charge.

Bob Novick, a legal counsel for Boeing, says that when the company went along with the 1992 agreement it was on the understanding that over time Airbus would wean itself from launch aid. But by 2004, despite Airbus's control of more than half of the global market in large commercial aircraft, Boeing could see no sign of that. The giant A380, which was made possible only by $3.5 billion in launch aid from France, Germany, Spain and Britain, and was designed to kill off Boeing's 747, was about to be rolled out.

Boeing was unhappy about the threat to the 747, its venerable cash-cow. But its main priority was to try to stop Airbus getting another slug of launch aid for its proposed A350, a potential competitor to both the American firm's highly successful 777 and larger versions of its new lightweight all-composite 787. Whereas Boeing felt it was betting the company on the 787, it believed that Airbus could develop its rival aircraft with far less financial risk and lower capital costs.

In addition to a claimed cumulative benefit of more than $100 billion from launch aid over 20 years, Boeing says that Airbus has also been the recipient of other handouts including funding for roads and runways it relies on and soft loans from the European Investment Bank. Boeing puts the combined value of all the subsidies Airbus has received at $205 billion.

Europe's response was to lodge a counter-complaint alleging that Boeing gets an array of subsidies from different American agencies ranging from America's space agency, NASA, to the Export-Import Bank of the United States (known as "Boeing's Bank") as well as tax breaks from several states. Europe puts Boeing's subsidy haul at only $24 billion over the past two decades and up to 2024, but says that using America's methodology, the figure would be nearer to $305 billion.

Europe also complains that Boeing has received launch aid from Japan, where large parts of the 787, including most of the wing, are made. It estimates that up to $7 billion-worth of government aid of one kind or another has gone into the 787. The boss of Airbus, Tom Enders, describes the 787 as the most heavily subsidised civil aircraft in history. Airbus also notes that since 1992 it has paid governments 40% more than it has received from them, thanks to interest and royalties on successful designs developed

with state aid. In an average year it repays about $500m.

The WTO's ruling on Europe's complaint should come within the next six months. It would not be surprising if both complaints were upheld, at least in part. Both parties say they are willing to negotiate a new deal limiting subsidies and making those that remain more transparent. That would send out a message to other countries (Russia and China) wanting to muscle in to the large commercial aircraft market. But both sides also want to see who comes out of the WTO process worst before starting talks.

Unfortunately, there will be plenty of opportunities to escalate hostilities in the meantime. In the next few weeks European governments are expected to agree to give some €3.5 billion ($5 billion) in launch aid for the A350. Boeing describes it as a "provocative" move, but an Airbus spokesman says the aid is not in doubt and that Europe will not be "intimidated". Another bone of contention is the battle between Boeing and Airbus, with its partner Northrop Grumman, to supply America's air force with its next fuel tanker—a contract won by Airbus last year which is being fought over again after Boeing protested. The grounds for further complaint, and thus the opportunities for inflicting mutual damage, are immense.

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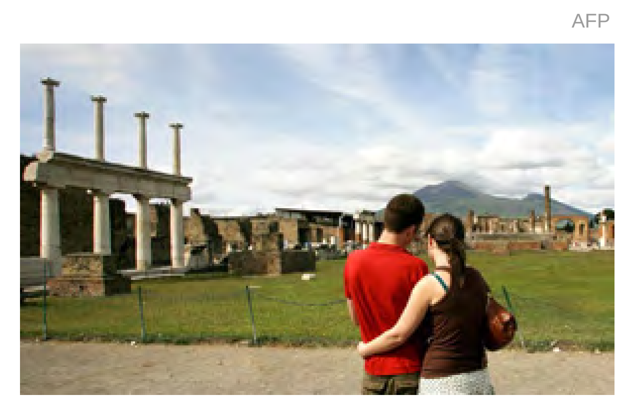
Tourism atrophies in Europe

Clouds over the Mediterranean

Aug 13th 2009 | PARIS AND ROME
From The Economist print edition

The recession clobbers one of Europe's biggest industries

AFP



Another disaster in Pompeii

HOW badly is the recession hurting Europe's tourism industry during the all-important summer holidays? The outlook is grim, judging by the trend set earlier in the year. After slipping in the second half of 2008, passenger numbers in Italian airports fell by 13.4% in the first quarter of this year. Spain recorded a similar fall between January and June, with airports on Lanzarote (down 19.1%) and Tenerife (down 17.8%), two popular holiday islands, losing more than most. The French Riviera is suffering, too: Nice airport reported a drop of 8% in passengers during the first half of the year. Firms have slashed travel budgets, families are spending less on leisure and Europe's airports are feeling the pain.

For hotels as well, the recession is biting in France, Spain and Italy, Europe's biggest holiday destinations. During the first five months of the year, the number of overnight stays by foreign visitors in French hotels fell by 15.5%. The number of foreigners who visited Spain in the first six months was 11.4% lower than in 2008. The situation is equally grim in Italy, where overnight stays by foreign guests were 11.5% lower in the first half of the year. Bernabo Bocca, chairman of the Italian hoteliers' association, described the results as a debacle.

Many jobs are at risk. In 2007, before the recession struck, France boasted nearly 200,000 hotels, pensions, campsites, restaurants, cafés and travel agencies, which employed almost 900,000 people on average during the year and took in some €70 billion ($96 billion). Spain had about 293,000 firms, with 1.4m employees and a turnover of €80 billion. Around 270,000 firms work in tourism in Italy and Mr Bocca says the 15% drop in turnover expected this year will quickly lead to job losses. Rome's hoteliers' association fears its members will shed 10,000 jobs this year.

Italy has beaches, mountains and lakes, and claims more artistic treasures than any other country. But last year 7.4% fewer people visited the Doge's palace in Venice than in 2007, and attendance was down by 3.8% at Florence's Uffizi gallery and 12.4% at Pompeii. Yet some attractions hold their own. Disneyland Paris, Europe's biggest crowd-puller with 15.3m visitors in the year to last September, reported a slight pick-up in the next six months. But that was something of a pyrrhic victory. Occupancy at the park's hotels was 2.7 percentage points lower, average spending by visitors fell by 3.7% and revenues by 7.3%. At museums, resorts and theme parks, expectations for this year and next are generally poor.

The euro's strength against the pound and the dollar adds to the problems of European tourism's big three. Britain sends more tourists to Spain than any other country, but the 6.1m that arrived between January and June were 16% fewer than during the same period of 2008. British and American tourists are the most numerous guests at expensive hotels in particular, so the luxury hoteliers of Paris and Rome are feeling their absence.

Mauro Cutrufo, Rome's head of tourism, believes the recession is an opportunity to push grandiose new schemes: marinas to match Monte Carlo, golf courses like those in Spain and theme parks to rival Disneyland. That is probably a mistake. However the world's economy fares, tourists are unlikely to abandon Mickey Mouse in favour of a Roman theme park. But foreigners will always want to visit the Colosseum and the Vatican museums, or make a pilgrimage to Paris to see the Mona Lisa.

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America's subsidies for filmmaking

The money shot

Aug 13th 2009
From The Economist print edition

Why government handouts to Hollywood are growing

WITH its deserts and its slight air of decay, New Mexico is a good place to shoot a post-apocalyptic action film. But the state's natural charms alone would probably not have been enough to lure the makers of "The Book of Eli". Broderick Johnson and Andrew Kosove, who are producing the Warner Bros film, say they were particularly enticed by New Mexico's generous production subsidies and interest-free loans.

All but seven of America's 50 states now offer incentives to lure filmmakers. Some states refund a portion of in-state production costs, which may include actors' salaries. Others issue rebates against state taxes that can be sold to local residents. The club is growing quickly. California, which resisted subsidies for years, recently approved its first clutch of recipients. Kentucky is considering its first application. With banks and hedge funds virtually out of the game, state governments are now the most important external source of funding in the film business.

Public largesse has led to some odd artistic decisions. "Gran Torino", a story that originally revolved around Minnesota's distinctive community of Hmong immigrants, was transplanted to Michigan to take advantage of that state's subsidies, which can amount to 42% of production costs. The forthcoming "Battle: Los Angeles" will be filmed mostly in Baton Rouge, Louisiana—a reversal of the tradition by which southern California stands in for everywhere else.

Studies commissioned by the states tend to show a healthy return on investment. Filmmakers have certainly learned to follow the money: California's share of big-studio productions dropped from two-thirds in 2003 to less than one-third in 2008 as its politicians dithered over subsidies. It is also likely that subsidies have helped America compete with Europe and Canada, although the weak dollar has probably done more to restrain what is known as "flyaway production".

The continuing bidding war is likely to result in diminished returns for the states. Michigan's subsidies, once considered improbably lavish, may soon be matched by Washington, DC. Alaska has approved a 44% rebate, although production companies must film in rural areas during the state's gruelling winter to qualify for the full sum. Whatever the benefit to the states, however, the subsidies are becoming ever more important to Hollywood.

But as state budgets tighten, a backlash is gathering. This summer Indiana and Wisconsin reduced their rebates. A bill to do the same is before the Michigan legislature. In the Midwest the surge in foreclosures and the collapse of traditional industries has hardened hearts. Jud Gilbert, a Michigan state senator who opposes film subsidies, points out that if he could offer a 42% rebate on car production, that industry would not be in crisis.

Yet a broad retreat from film subsidies is unlikely. Some of the first places to offer rebates, such as New Mexico and Louisiana, now have impressive sound stages and a deep pool of production workers. States that want to compete with them will have to be extremely generous. And big studios and independent outfits are sharply trimming their film output in response to the credit crunch and a faltering DVD market. As the supply of work shrinks, the squabbling will only intensify.

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Online auctions

Mind the pennies

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The rapid spread of "entertainment shopping" spurs indignation

Illustration by Claudio Munoz

IT IS a familiar format: the stopwatch on the website counts down the time remaining to make bids in the online auction. The price slowly ticks up. Participants monitor the site, hoping to secure a great bargain. But there is a twist: it is the website itself that provides the goods being sold, and the prices only rise by a penny or two per bid. Each new bid, however, extends the length of the auction by a few seconds. That means that competition is fierce and protracted, but winning bids are often absurdly low, even by the standards of online auctions: a flashy new television for $3, say, or a laptop for $20. These enticing offers lure buyers, who must pay a fee of a dollar or so to place each bid. This format, known as "entertainment shopping", has become so popular that it has spawned a host of websites.

"People will try it because they want to get a good deal," says Lael Sturm, a co-founder of one such site, GoBid.com. "But it's the experience that brings them back—they are in it for the thrill of winning." GoBid, like most of its rivals, is new. It launched officially in America in April. Swoopo, the most prominent site, was founded in Germany in 2005 but in the past two years has expanded into Austria, Canada, Spain, Britain and America. It plans to set up a South Korean website before the end of the year.

Swoopo has doubled its revenue every year for the past three, attracting 2.5m registered users along the way. Last year it says it made a profit on revenue of €22m ($32m). But whereas it took about three months for Swoopo's first competitor to appear, now, says Gunnar Piening, the firm's boss, "there is a new one emerging every week." The format is so popular that you can buy software online to launch a penny-auction website.

Running a profitable penny auction is difficult, however. If auctions attract too many people, participants may lose heart because there are too few winners. But small auctions can lead to low winning bids, and thus less profit. The weight of competition adds to the pressure. And then there is the indignation that penny auctions provoke. Last year one blogger declared that Swoopo was "about as close to pure, distilled evil in a business plan as I've ever seen".

Howard Hartenbaum, of August Capital, a venture fund that has invested in Swoopo, shrugs off the fuss. He points out that Skype, another firm he backed, also caused some controversy. But he concedes that "if the customer believes there is a problem, there is a problem". So last month Swoopo began letting failed bidders purchase the item they wanted at a discount equivalent to the amount they spent bidding. This "Swoop it Now" feature should raise revenue, but will cut into margins. But "to be a substantial business," says Manfred Hasseler, Swoopo's founder, "you have to make as many people happy as possible."

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The outlook for jobs in America

Help not wanted

Aug 13th 2009 | NEW YORK
From The Economist print edition

How quickly will firms start hiring again as the economy recovers?

AP



A rare sight

THERE have been times when a sharp rise in the productivity of American business would have been greeted as unambiguously good news—a miracle, even. But the announcement on August 11th that productivity had jumped by 6.4% in the second quarter, and had increased by 1.8% compared with a year earlier, caused as much consternation as celebration.

In past downturns productivity has tended to fall, because firms have been slow to make cuts to their workforce. This time, the worry is that rising productivity indicates they have cut too aggressively, shedding muscle as well as fat. But that thought, in turn, is giving rise to some optimism that employment will rise faster than usual once the economy starts to recover, as firms rush to repair the damage done by their overzealous axe-wielding.

Alas, for America's unemployed masses, now 9.4% of the workforce, this is probably wishful thinking. A few firms have shed too many jobs, but most have not, says Grant Freeland of the Boston Consulting Group. Chrysler, for example, is one firm that has overdone it (as have many of the rising number of firms filing for bankruptcy). The carmaker will need "new talent if it is to survive", he thinks, but most firms have just "taken fat off the top". Late last year they resorted to modest cuts combined with trimmed bonuses, offers of shorter working hours or unpaid holidays and so forth. In the first half of this year, they started making bigger cuts.

Firms have historically been reluctant to shed managers, partly because they do not want to lose anyone talented enough to have been promoted to a senior job, and partly because the people making the cuts often know their victims. "There have been more job cuts at higher levels in the past four months," says Jeff Joerres, the boss of Manpower, an employment-services firm that includes the world's largest outplacement business, advising firms on how to handle job cuts. He believes companies are becoming more thoughtful about job-cutting, actively restructuring instead of just slashing the workforce across the board. In the long run this may prove a boon for American firms, which have far more freedom to choose which workers to dismiss than their European counterparts.

Firms now have a much better understanding of their employment needs than in the past, says Mr Joerres, who attributes this in part to vastly improved computer systems. These help firms keep much closer track of orders, inventories and the like, and so help them to determine faster and more accurately when extra staff are needed. That might fundamentally alter how they think about recruitment as the economy recovers.

In the past, once economists had declared a downturn over, firms would typically start hiring in the expectation that demand was about to surge. These days, however, says Mr Joerres, "firms will no longer

hire in anticipation; they will wait to respond to actual changes in demand.” Ominously, he says that many of Manpower’s American clients have been delaying another round of lay-offs in the hope of an increase in demand after the summer holidays. If that demand does not materialise, the next lot of cutting could be the most painful yet.

If big firms are unlikely to start hiring again briskly whenever the economy revives, what about smaller ones, which have, after all, long been a far greater source of new jobs? Certainly, the downturn has led to a sharp increase in the number of people starting new businesses. However, most of these start-ups will struggle to obtain the loans they need to grow, thanks to the shortage of credit amid the detox of the financial system. The latest Small Business Economic Trends Survey, published by the National Federation of Independent Business on August 11th, found that small-business owners became even gloomier in July. The margin of those planning to cut jobs over those planning to add them grew. For the time being, sadly, rising productivity in America looks a far safer bet than rising employment.

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Lenovo bets on China

Where the heart is

Aug 13th 2009 | HONG KONG
From The Economist print edition

China's biggest computer-maker returns to its roots

IT WAS once seen as a model for Chinese firms eager to take on the world, but is now considered more of a cautionary tale. When Lenovo bought IBM's ailing personal-computer (PC) division for $1.75 billion in 2005, it transformed itself from the biggest maker of PCs in China into the third-biggest PC-maker in the world and one of the most ubiquitous Chinese brands. But earlier this month the firm reported its third quarterly loss in a row, of $16m. It had lost a total of $361m in the previous two quarters. It is also losing market share: Taiwan's Acer has surpassed it to become the world's third-biggest computer-maker. Success in China, it seems, is no guarantee of success abroad.

Sluggish demand in America and Europe has hit Lenovo hard. Its sales in those markets fell by 17% in the most recent quarter compared with the same period last year. By contrast, Lenovo powered ahead in its home market. It shipped 15% more PCs than it did a year ago in mainland China, which accounted for 48% of its sales. Although the firm had pinned its hopes on international growth, it was China's effort to boost domestic consumption through a massive fiscal stimulus that prevented a worse outcome.

In addition to the global economic downturn, the botched integration of IBM's PC business has been weighing on Lenovo's results. In announcing the deal, Lenovo executives spoke excitedly about creating the first truly global Chinese company. Its chairman at the time, Yang Yuanqing, moved with his family to America. Lenovo also appointed William Amelio, a veteran of Dell, a rival PC-maker, as its new boss. Putting a Westerner in charge, the firm reckoned, would send a bold message to staff and customers alike of its determination to internationalise.

Mr Amelio did manage to stanch the losses inherited from IBM, thanks in part to the booming world economy. But the good times ended in mid-2008 amid the credit crunch and the subsequent pullback in business spending. Lenovo is now paying a heavy price for failing to address its new division's reliance on Western companies.

Perhaps distracted by the takeover, it was unprepared for the PC market's shift to consumers, says Bryan Ma of IDC, a research firm. With losses mounting, Lenovo in January announced a restructuring plan to cut costs by $300m by March 2010. It said executives would face pay cuts and 2,500 employees (11% of its workforce) would lose their jobs. In February Mr Yang replaced Mr Amelio and Lenovo's founder, Liu Chuanzhi, became chairman again. On August 10th the Chinese Academy of Sciences, which owns 65% of Lenovo's parent, Legend Holdings, revealed that it was looking to sell almost half its shareholding to a Chinese buyer to help improve the company's governance.

Lenovo is returning to its roots. The reappointment of Mr Liu, who oversaw the firm's transition from a local distributor of foreign PCs to the biggest domestic manufacturer, is a clear sign that Lenovo believes its best chance of revival lies in fast-growing China. What is more, the Chinese government has earmarked some of the 4 trillion yuan ($585 billion) stimulus to subsidise the purchase of computers by people in rural areas. Lenovo is introducing more than a dozen models priced below 3,500 yuan to cater to this market. Investors heartily approve: Lenovo's shares are up 76% this year.

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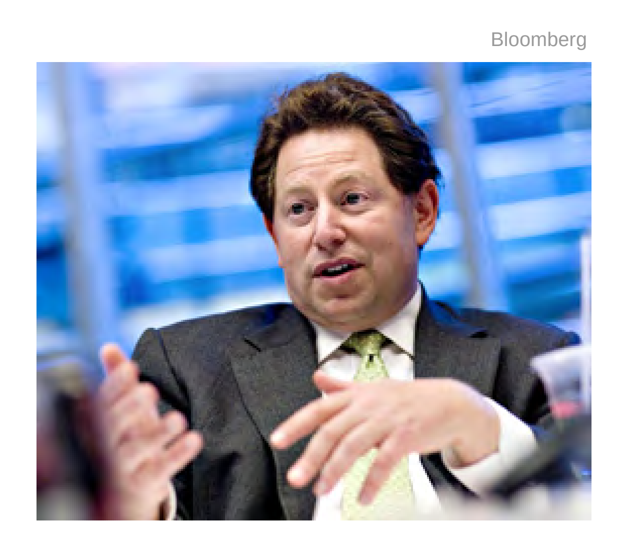
Face value

Top of his game

Aug 13th 2009
From The Economist print edition

Bobby Kotick of Activision Blizzard has helped the video-game industry grow up

Bloomberg



LIKE many teenagers, Bobby Kotick was drawn to video games when they first appeared in the 1970s. He had an Atari, with its chunky plug-in cartridges and blocky graphics, and he liked to play "Defender" at the arcade. The young Mr Kotick also had an entrepreneurial streak: he sold bagels and soft drinks to people waiting in line for petrol during the 1979 energy crisis. How appropriate, then, that he has ended up as the boss of Activision Blizzard, the world's largest publisher of video games.

So did Mr Kotick and the industry grow up together? Not quite. It would be more accurate to say that Mr Kotick was one of the people who helped the chaotic games business grow up, by applying a more rigorous approach to management. Many gamers dislike him, complaining that his bean-counting approach stifles creativity. But there is no denying his ability to get results: earlier this month his firm reported impressive sales and higher than expected profits of $195m for the three months to June.

Mr Kotick's big break came in 1983, when he was a student at the University of Michigan. He was about to leave for New York to meet potential investors in a firm he was setting up to make software for the Apple II computer when he met Steve Wynn, a casino tycoon, at a party. Mr Wynn was also heading to New York and offered Mr Kotick a lift in his private jet. "I went with him on the plane, and asked him how he got started," Mr Kotick recalls. Mr Wynn explained that early in his career he had been helped out by E. Parry Thomas, a legendary Las Vegas banker, who helped finance Mr Wynn's takeover of the Golden Nugget casino. Mr Wynn had promised Mr Thomas that he would, in turn, give a helping hand to a young entrepreneur some day. He offered to invest in Mr Kotick's new company, and ended up writing him a cheque for $300,000. Mr Wynn became his mentor, and was involved in 1991 when Mr Kotick took over Activision, a failing games publisher founded by former Atari employees.

The problem with the video-game industry at that point, says Mr Kotick, was that it lacked discipline. "We needed a balance", he says, "between people who would be creative and entrepreneurial, and people who knew processes." He brought in managers from packaged consumer-goods firms, including Procter & Gamble and Pepsi, to oversee the development of new games and to provide expertise in consumer testing and marketing. But he realised that it was also important to maintain a creative environment for designers. "In our business the key is that certain things lend themselves well to process, and certain things don't," he says.

Through both growth and acquisitions he built Activision into a gaming giant. Today it is known for the "Tony Hawk" skateboarding games, the "Call of Duty" series of military shoot-'em-ups, and its "Guitar Hero" games, in which players must press buttons on a plastic, guitar-shaped controller in time with blaring rock music. Each of these is a brand in its own right and has spawned numerous versions and

sequels. This has led to criticism that Activision's approach is too dependent on exploiting and re-exploiting franchises. But Mr Kotick vigorously denies that his company fails to innovate. "A small segment of very vocal gamers say everything has to be new and different every year," he says. "Actually, people are happy with existing franchises, provided you innovate within them." The trick, once again, is to strike a balance: between the familiarity of a trusted brand and "innovative and inspiring" new features.

Mr Kotick's greatest coup was the merger of Activision with the gaming arm of Vivendi, a French media conglomerate, completed last year. Vivendi's main gaming asset was Blizzard, the firm behind "World of Warcraft", a wildly popular online fantasy game played by 12m paying subscribers. Although the deal gave Vivendi a 54% stake in the merged firm, Activision's management team was kept in place to run it. Mr Kotick had wanted to get his hands on "World of Warcraft" for some time, because its subscription-based model provides regular income, in contrast to the sporadic, release-driven proceeds from games sold in shops. More than half of Activision Blizzard's operating profit now comes from subscriptions, he says: "'World of Warcraft' is the most stable form of profitable revenue in the industry."

Let's get physical

As the industry moves towards a greater reliance on subscriptions and online gaming, Mr Kotick's firm is on the right side of the trend. "Guitar Hero", meanwhile, was an early example of "physical gaming", in which players use special controllers to get closer to the on-screen action—another big industry trend, encouraged by the success of Nintendo's Wii console, with its motion-sensitive controls. Activision was quick to recognise that the Wii would broaden the appeal of gaming, and it is now the biggest producer of games for the Wii after Nintendo itself. "We are seeing new audiences emerge because of the physical nature of the experience," says Mr Kotick. His firm's latest entries in the physical-gaming arena are "DJ Hero", a music game in which the player handles a turntable, rather than a guitar, and a new version of "Tony Hawk" with a motion-sensitive skateboard control.

So what games does Mr Kotick like to play at home? These days, he admits, he only indulges in the odd bout of "Guitar Hero" with his children. When he used to play more games, he says, he would find himself trying to tweak his firm's products to accord more closely to his own tastes. Such decisions are best left to product managers, he insists, who combine their own judgment with feedback from focus groups. The trick is knowing which bits of feedback to ignore. "That's the delicate balance," he says. Mr Kotick looks rather incongruous as he proudly shows off his firm's new skateboard controller, putting it down on the floor and grinning as he wobbles to and fro. As he knows better than anyone, success in video-gaming is all about balance.

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Emerging Asian economies

On the rebound

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From The Economist print edition

Asia's emerging economies are recovering much more quickly than economies in other parts of the world. Can they keep it up?

Illustration by Bill Butcher



MORE green shoots have appeared in America in recent weeks, but they are nothing by comparison with the lush jungle sprouting in the East. Asia's emerging economies probably grew at an average annualised rate of over 10% in the second quarter, while America's GDP fell by 1%. In 2009 as a whole, recent forecasts suggest that emerging Asia could grow by at least 5%, while the G7 economies contract by 3.5%. The growth gap between the two has never been wider. How have these export-dependent economies managed to decouple from the developed world? And can their recovery last?

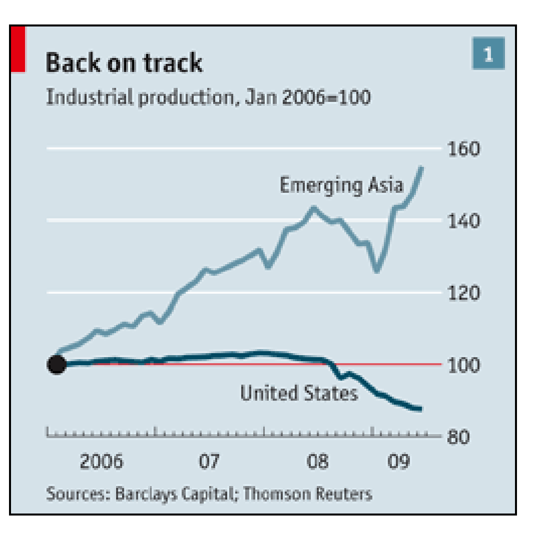
Average growth figures conceal big differences within Asia over the past year. China, India and Indonesia were among the few economies in the world that continued to expand throughout the global downturn (though China's virtually stalled late last year). But the smaller, more open Asian economies were badly hit. Between September and March real GDP fell by an average annualised rate of 13% in Hong Kong, Malaysia, South Korea, Singapore, Taiwan and Thailand.

Yet the countries that have so far published second-quarter GDP figures show an impressive bounce. Comparing the second quarter with the first at an annualised rate, China's GDP grew by 15%, South Korea's by almost 10%, Singapore's soared by 21% and Indonesia's managed a respectable 5%. Other countries in the region are also likely to show a rebound. It is true that output in South Korea and Singapore was still lower than a year earlier, but quarterly changes are more useful for spotting turning points—and this is how growth rates are most commonly measured in America.

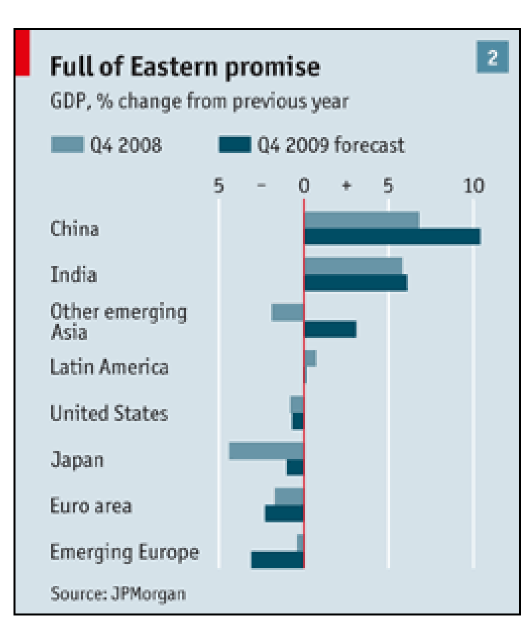
The revival in emerging Asia's industrial production is even more impressive, jumping by an annualised rate of 36% in the second quarter. According to Barclays Capital, emerging Asia is the only region in the world where output has regained its level before the crisis (see chart 1). This is largely due to China, where industrial production rose by 11% in the 12 months to July, but all the Asian countries have seen a strong pick-up. In contrast, up to June, America's production continued to fall.

The sharp "V" shape of this cycle, and the fact that GDP started the year well below the average level in 2008, means that growth

rates for 2009 as a whole could give a misleading picture. Take Taiwan: JPMorgan predicts that its GDP in 2009 will be 3.8% lower than in 2008, implying another dismal year. But this forecast also implies that GDP will grow by a brisk 5.4% in the year to the fourth quarter. By this measure, Asia's emerging economies are clearly leading the global recovery (see chart 2). Even if America's economy grows during the second half of this year, it is still expected to end the year smaller than it was at the start.



Asia's bounce has taken many forecasters by surprise. In May, for example, the IMF predicted that Asia's recovery was likely to be "tepid" because the developed economies—and hence demand for Asian exports—would remain weak. Forecasters always seem to underestimate the ability of the Asian tigers to rebound from recessions. During East Asia's financial crisis in 1997-98, for example, countries across the region were forced to devalue as a result of large current-account deficits and speculative attacks on their currencies. This caused firms' foreign-currency debts to swell in local terms, resulting in widespread bankruptcies and bank failures. In 1998 the real GDP of Thailand, Indonesia and South Korea fell by an average of 10%.



Many foreigners concluded that Asia's economic success had been a complete sham, based on governments pouring cheap money into favoured firms. Over-borrowing and over-investment had artificially boosted growth, it was argued; doomsayers predicted a decade of lost growth. Instead, the tigers came roaring back. At the end of 1998 *The Economist*'s poll of forecasters predicted that South Korea would shrink again slightly in 1999. Its actual growth turned out to be a stunning 9.5%. It was true that Asia's strong growth had concealed wasteful investment, inadequate bank regulation and corruption, but the key ingredients of growth—rapid productivity growth, relatively open markets and a high saving rate to finance investment—remained in place. That helps explain why the East Asian economies recovered more quickly than many expected.

A case of Asia vu

Likewise, when the global information technology bust dragged Asia into recession in 2001, forecasters turned out to be much too gloomy about Asia's prospects. Once again, emerging Asia bounced back fairly briskly. Westerners have always been too quick to pronounce the death of the Asian economic miracle. This may be wishful thinking, but it also reflects some misunderstandings about the ingredients of Asia's success. This year it was widely predicted that Asia's economies would not recover until after America and Europe had revived. Yet Asia's supposedly export-dependent economies have resumed growth before the rest of the world. How can that be?

Sceptics argue that the pick-up simply reflects a temporary boost from rebuilding inventory, with no real increase in demand. Firms had cut production to below the level of sales in order to shed excess inventories, so now they need to reopen factories. This may be a factor in some countries, but in others firms are still running down their stocks.

In South Korea the decline in inventories accelerated in the second quarter, and the leanness of stocks bodes well for further gains in production over the rest of this year. Instead, the recovery has been led by investment and consumer spending. South Korea's private consumption rose by an annualised 14% in the second quarter. In China fixed investment (on a GDP-consistent basis) is running more than 20% higher than a year ago, real consumer spending in urban areas is up by almost 11% and car sales have surged

by 70%.

One reason why Asia's emerging economies have been able to rebound well before those in the rich world is that their downturn was caused only partly by the slump in America. In 2008 domestic spending was squeezed by higher prices for oil and food (which account for a much higher share of household budgets than in other countries) and by tighter monetary policies, aimed at curbing inflation. China's growth, for instance, began to slow well before global demand stumbled, as tight credit policies to prevent the economy overheating caused the property market and construction to collapse.

Across the region, aggressive fiscal and monetary stimulus has helped revive domestic demand. Asia has had the biggest fiscal stimulus of any region of the world. China's package grabbed the headlines, but South Korea, Singapore, Malaysia, Taiwan and Thailand have all had a government boost this year of at least 4% of GDP. Most Asian countries, with the notable exception of India, entered this downturn with sounder budget finances than their Western counterparts, so they had more room to spend. Bank of America Merrill Lynch forecasts that the region's public debt will rise to a modest 45% of GDP at the end of 2009, only half of the average in OECD countries.

Moreover, pump-priming has been more effective in Asia than in America or Europe, because Asian households are not burdened with huge debts, so tax cuts or cash handouts are more likely to be spent than saved. It is also easier in a poorer country to find worthwhile infrastructure projects—from railways to power grids—to spend money on.

In China the easing of credit has been even more important than its fiscal stimulus. Although lending slowed sharply in July, new lending by banks in the first seven months of this year was almost three times its level a year earlier. And across the whole of emerging Asia, cheaper money has been more potent in lifting spending than in the West. This is because, unlike in America and Europe, local financial systems are not crippled, so banks are able to lend more. And since Asian households and firms had not previously been on a borrowing binge (South Korea is an exception), they can afford to borrow more.

Growth rates will almost certainly moderate after the second quarter's astonishing bounce. Even so, Mike Buchanan, an economist at Goldman Sachs, has raised his forecast for GDP growth in emerging Asia to 5.6% for 2009 as a whole and 8.6% in 2010. He expects China to grow by a breathtaking 9.4% this year and 11.9% next.

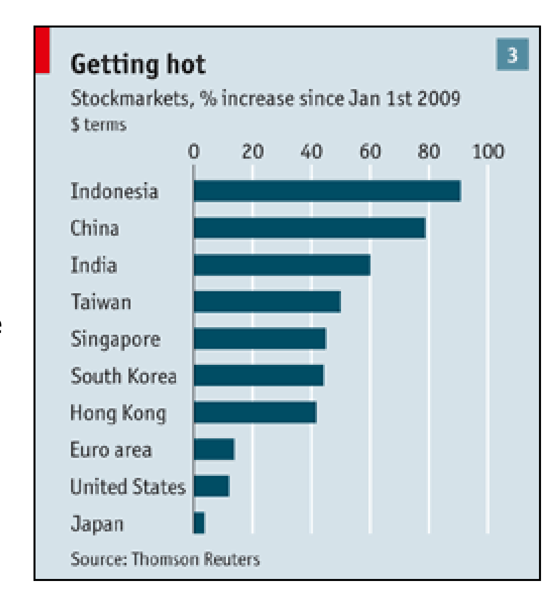
India's GDP is forecast to grow by a more modest 5.8% in this fiscal year (ending March 2010). Exports accounted for only 15% of India's GDP in 2008, compared with 33% in China, so India should have been much less affected by the global downturn. But because of its dire fiscal finances (a budget deficit of 10% of GDP last year), the government has had much less room to spur growth. The poor monsoon rains are also expected to reduce farm output this year. However, Mr Buchanan expects growth to increase to 7.8% next year.

Bubbling up

Even though these economies are only just starting to feel the upturn, policymakers now face a difficult problem: how to sustain a robust recovery without blowing up bubbles. There are growing concerns that a flood of liquidity is fuelling asset-price bubbles, which could destabilise economies when they burst. In China share prices have almost doubled since their trough last November, and most Asian countries have seen gains of around 50% or more since the start of the year (see chart 3). After falling last year, house prices are now rising rapidly in Hong Kong, Shanghai, Seoul and elsewhere. Home sales have surged by 70% in value in China over the past year. According to one estimate, one-fifth of all new lending this year in China has gone into the stockmarket or property.

Asset prices could rise much further. Despite the recent gains, average house prices in most countries are barely higher than a year ago. And although shares are starting to look pricey, China's stockmarket is still 47% below its 2007 peak. But the lesson from America in recent years is surely that it is better to prevent bubbles forming. Asia's monetary conditions are too loose now that economies are reviving; central banks need to raise interest rates. But with rates close to zero in the rich world, and likely to stay there for a while, this would lure in foreign capital, adding to domestic liquidity. Capital is already rushing in, attracted by the region's growth, which is faster than the rest of the world's.

The basic problem is that although the Asian economies have decoupled from America, their monetary policies have not. In a world of mobile capital, an economy cannot both manage its exchange rate and control domestic liquidity. By trying to hold their currencies down against the dollar Asian economies are, in effect, being forced to shadow the Fed's monetary policy even though their economies are much stronger. Foreign-exchange intervention to hold down their currencies causes domestic liquidity to swell. Consumer-price inflation is not an imminent threat, because prices are falling in most Asian countries. Chinese consumer prices fell by 1.8% in the year to July. But asset prices look dangerously frothy. The obvious solution is to let exchange rates rise, but with exports still well below last year's level, governments are reluctant to set their currencies free.



Making it stick

Several central banks in the region, including the People's Bank of China, the Bank of Korea and the Hong Kong Monetary Authority, have given warnings about the risk of asset bubbles. But there is unlikely to be any significant policy tightening before next year, because boosting growth remains governments' main priority. Indeed, the wealth effects of higher asset prices will help lift spending. Ample liquidity is therefore likely to continue to stoke asset prices. Andy Rothman, an economist at CLSA, a brokerage, predicts the "biggest round of asset-price inflation China has experienced since the command economy was dismantled".

Its credit boom is clearly unsustainable, but China is unlikely to hit the monetary brakes until inflation turns positive and its year-on-year GDP growth tops 10%. Instead, policymakers will try to contain the bubble by tightening lending standards. For example, China's banking regulator has warned banks to stick to rules on mortgages for second homes, which require a down-payment of at least 40% of a property's value. It has also ordered banks to ensure that lending goes into the real economy, not shares.

Fiscal stimulus and the wealth effect of rising asset prices can provide only a temporary prop to domestic spending. Nor can Asia rely on a strong rebound in exports to America, where spending is likely to remain sluggish over the next few years as households are forced to save more in order to repay debt. In the longer term, Asia's growth needs to come more from domestic demand rather than exports.

However, the standard policy prescribed by Westerners—Asian households must save less and spend more—is too simplistic. In China private consumption is indeed unhealthily low, at only 35% of GDP. But the average for the rest of Asia, at 58% of GDP, is not much lower than the OECD average of 61%. South Korean households, which have reduced their saving rate from 23% of disposable income in 1998 to only 3% last year, can hardly be accused of being overly thrifty.

In Indonesia, Malaysia, the Philippines, Taiwan and Thailand it is instead investment that looks too low. Investment as a percentage of GDP is little higher than in many rich economies, even though investment opportunities in a developing country should be far greater. For example, Malaysia's investment has fallen from 43% of GDP in 1997 to only 19% last year, less than in the euro area or Japan and well below China's 44%. Weaker investment is one reason why the trend growth-rates of some Asian economies have slowed over the past decade.

The appropriate measures needed to strengthen domestic demand therefore differ across the region. Although China's goal should be to consume more, some of the other Asian economies need to invest more. That will require an improved regulatory environment, a crackdown on corruption, better infrastructure and—not least—greater political stability.

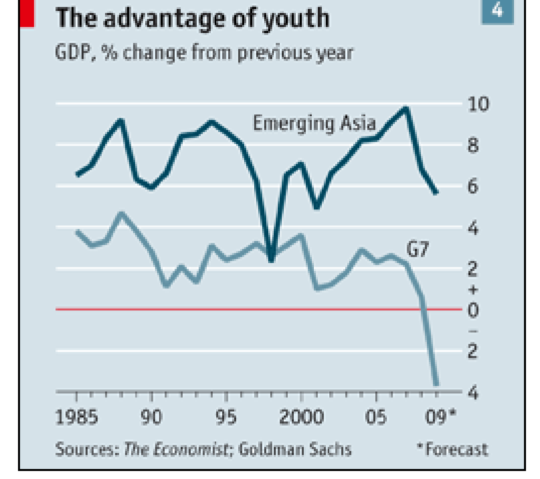
Even in countries like China, where low consumption is the main culprit, the necessary reforms are more complicated than the standard Western advice that the government needs to spend more on health care and welfare support to encourage households to save less. Companies, not households, have accounted for the bulk of the rise in saving across Asia over the past decade. Households' spending has fallen as a share of GDP, not because they are saving a lot more, but because their share of national income has shrunk as that of corporate profits has grown.

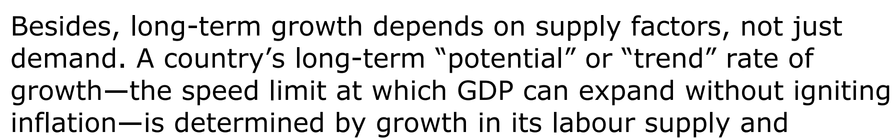
To lift private consumption, governments therefore need to increase households' share of national income by encouraging more labour-intensive services, rather than favouring capital-intensive manufacturing

industries with subsidies and undervalued exchange rates. Recent estimates suggest that Asian currencies are among the most undervalued in the world. Stronger exchange rates would help shift growth away from exports and boost households' real spending power.

Mind the gap

The gap between growth rates in emerging Asia and the G7 is forecast to rise to a record nine percentage points this year (see chart 4). But what of the future? Pessimists argue that Asia's growth over the coming years will be much slower than before the global crisis because its main engine of growth, exporting to America, has broken down and it will take years to find a replacement. But this may overstate the importance of America to the Asian tigers. Between 2001 and 2006 (when America's trade deficit peaked), the increase in emerging Asia's trade surplus with America accounted for only 6% of the region's GDP growth. If those exports cannot be replaced by domestic demand, growth will be slower, but not massively so.





Besides, long-term growth depends on supply factors, not just demand. A country's long-term "potential" or "trend" rate of growth—the speed limit at which GDP can expand without igniting inflation—is determined by growth in its labour supply and productivity. The global financial crisis should not noticeably reduce productivity growth in emerging Asia. Indeed, recent increases in infrastructure spending across the region could boost productivity by reducing transport costs, especially in places such as inland China.

In America and many other rich countries, by contrast, potential growth rates are likely to fall over the next decade as soaring government debt and hence higher taxes blunt incentives to work and invest, the lingering credit crunch dampens investment, and increased government regulation deters innovation. All this could reduce productivity growth at a time when labour forces in these countries will be growing more slowly or even shrinking.

The tigers are unlikely to return to their breakneck growth rate, which averaged 9% during the three years to 2007. But this exceeded their safe speed-limit. Emerging Asia as a whole might enjoy annual growth of 7-8% over the next five years, at least three times the rate in the rich world. The sharp downturn in Asia late last year painfully proved that the region was not immune to America's downfall. But the speed and strength of its rebound, if sustained, show that it is not chained to Uncle Sam either. If anything, the crisis has reinforced the shift of economic power from the West to the East.

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AIG, Fannie Mae and Freddie Mac

The toxic trio

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American taxpayers are ploughing billions in. Will they get their money back?

Illustration by S. Kambayashi



FORGET the banks and the carmakers. The biggest bets that American taxpayers have made are on three less famous firms: American International Group (AIG), an insurer, and Fannie Mae and Freddie Mac, two mortgage-finance agencies. The state now owns about $170 billion of shares in banks. It has so far invested over $160 billion of equity in the toxic trio, and this number is likely to rise towards $300 billion. Include other kinds of help, such as loans, and the total pumped into the three firms could eventually reach $800 billion (see table), or 6% of GDP. "I had no idea what I was in for," admitted Edward Liddy this month as he stepped down after a gruelling year running AIG. Americans must feel the same way.

The case that was made to taxpayers last year for bailing out the three is intact. Through its derivatives activities and giant insurance business, AIG was so entangled in the financial system that it could have brought it down. Fannie and Freddie, which own, guarantee and help securitise about half of American mortgages, were judged as vital to a healthy housing market. Banks and foreign governments held buckets of their paper, too, in the belief it had implicit state backing. Defaults would have badly hurt relations with China, the largest foreign-government creditor.

What has changed is the size of the bill. AIG's bail-out has been revised upward four times as its losses have mounted. "They tried to put on a band aid and then realised they needed a tourniquet," says Rob Haines of CreditSights, a rating firm. When the government first began to help the two mortgage agencies in July 2008, it said capital injections were "not something we expect". That looks like a bad joke now. The question is no longer whether the trio will receive vast sums, but whether taxpayers will get any money back.

Of the three firms, AIG represents their best hope, even though its credit spreads are still at levels that suggest a real risk of default. The government fired a blunderbuss of money at it, with six different categories of intervention (see table). Safest are probably the direct loans from the Federal Reserve, the commercial paper that the Fed has guaranteed and the loans that it is likely to make that are secured by life-insurance policies. These instruments are fairly high up the pecking order if the firm goes bust. The $25 billion preferred-equity stake that the Fed owns in two of AIG's insurance subsidiaries is also pretty safe: they may be worth as much as double that sum.

Black holes come in threes

State assistance, $bn

	Distributed	Maximum available
AIG		
Direct loans	20	35
Secured loans	*nil*	9
Commercial-paper lines	12	15
Loans to special-purpose vehicles	44	53
Equity stakes in two subsidiaries	25	25
Equity stake in AIG	43	70
Total	**144**	**207**
Fannie and Freddie		
Equity	98	400
Fed debt purchases	107	200
Total	**205**	**600**

Sources: Federal Reserve; Company reports; *The Economist* estimates

The danger to taxpayers comes in two forms. First, the Fed has lent $44 billion to two special-purpose vehicles, into which many of AIG's flakiest securities have been dumped, including derivatives written on structured-credit instruments. At the end of March these vehicles were $5.4 billion in the red: unless prices recover taxpayers will ultimately take the hit. Second, the Treasury has $43 billion of preferred shares in AIG itself. So far the firm's core book value (the value of its assets) is about equal to that, suggesting that the investment is covered.

The Fed has around 25 full-time staff sitting in AIG now, so its accounts should be more reliable. But even though AIG made a small profit in the second quarter, more losses are possible. It still has a giant portfolio of credit-default swaps that European banks use to game capital rules. These have not lost money yet, but remain a black box. And the government's long-term plan to raise cash by spinning off or selling the traditional insurance businesses could crystallise losses. Several AIG assets sold so far have ended up fetching less than book value.

These risks, though, pale into insignificance compared with Fannie and Freddie. The two have racked up colossal losses. As Wall Street ate into their securitisation business, they branched into buying debt securities worth some $1.6 trillion. Of this about $230 billion turned out to be toxic, with losses of almost $90 billion at market prices. Future pain will come from the traditional guarantee business. The pair have underwritten $4.8 trillion of mortgages between them and delinquency rates are rising along with unemployment. Impairments are likely to be only 4-5% of the total but that would be more than enough to sink the two agencies.

The government has agreed to fund these losses with equity injections of up to $400 billion. It has invested $98 billion so far, and Rajiv Setia of Barclays Capital thinks the total cumulative capital required will be $160 billion-200 billion. It could turn out worse. The book value of the two firms, using market prices and excluding the existing equity from the state as well as tax assets, showed a capital shortfall of $280 billion at the end of June. This sum is a proxy for how much taxpayers will lose unless prices recover.

Such massive insolvency makes it hard to restructure the two agencies. Right now they are staggering on in "conservatorship", a form of direct state control. The Treasury is backstopping their capital and the Fed is helping them refinance their debts by buying up to $200 billion of their bonds in the open market. Over time their holdings of securities will probably be wound down. The guarantee business will be harder to kill. The government plans to decide on Fannie's and Freddie's futures by February, but the agencies are likely to survive under state control or as co-operatives with state guarantees.

This extraordinary resilience reflects the widespread political lust in America for subsidising housing. Anyone who doubts this should look at Ginnie Mae, another fully state-owned agency which guarantees and bundles mortgages, usually of below-average quality, that are insured by the government. Fannie and Freddie are now being conservative about writing new business, but Ginnie is enjoying its own bull market, issuing guarantees at a furious rate. It is expected to have a trillion dollars outstanding by next year. "We are seeing a gravitation of the subprime universe from Fannie and Freddie to Ginnie", says Mr Setia. It will be a miracle if taxpayers get their money back from Fannie and Freddie. Worse, there is a chance the disaster will be repeated.

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Bankers' pay and the French

More égalité, less liberté

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France is pushing for a global crackdown on bankers' bonuses

Getty Images



ON AUGUST 6th France's prime minister, François Fillon, summoned the country's most senior bankers for a scolding after it emerged that BNP Paribas, its biggest bank, had set aside €1 billion ($1.4 billion) for bonuses so far in 2009. Bonuses are back in vogue throughout the industry but are proving particularly contentious in France. The leader of the opposition Socialist Party said the bonus plan was scandalous and BNP's lowest-paid employees protested outside its headquarters. France's bank bosses will get another drubbing over pay in a meeting with the president, Nicolas Sarkozy, on August 25th.

BNP can justly claim to have been unfairly treated. Its bonus pool is small by comparison with sums recently announced by some foreign rivals. As the Bank of France pointed out, the bonus plan complies with rules introduced in February at the behest of Christine Lagarde, the finance minister, to ensure that the structure of bankers' compensation does not encourage excessive risk-taking. BNP and its peers have agreed to stop offering guarantees of bonuses beyond one year, to pay bonuses out of profits rather than revenues, to adjust payments to reflect the risks taken and to defer a share of variable compensation so that bonuses can be clawed back if losses materialise.

Public anger is fuelled by the fact that the government injected a total of €10.5 billion into the six biggest banks in 2008; more money was made available this year. In most cases, however, banks accepted government funds not to stave off collapse but to boost lending to the real economy. And the government is earning interest at a tidy 8% on its money. "The whole affair shows how the French suffer from a lack of understanding of economics and of banking in particular," says Guillaume de Saint Seine, a banker in the Paris office of Leonardo & Co, a boutique investment bank.

French bank bosses may yet have some complaints of their own for Mr Sarkozy when they meet. They hoped other countries would implement similarly tough new rules on bankers' pay, as recommended at the meeting of G20 countries in London in April. Yet some foreign competitors are once again offering multi-year guaranteed bonuses to lucky employees. Barclays Capital, the investment-banking division of Barclays, has admitted awarding such packages to a handful of senior staff. Citigroup, Bank of America and Nomura are also reportedly offering bonuses guaranteed for more than one year.

"If the new guidelines on pay remain specific to France, that could be an issue for the competitiveness of French banks," says Philippe Tibi of AMAFI, a trade group for the French securities industry. Ms Lagarde plans to use the next G20 meeting in Pittsburgh in September to push other countries to clamp down on controversial pay practices. On August 12th Britain's Financial Services Authority published a long-awaited code of practice on remuneration which, among other things, frowns on bonuses that are guaranteed for more than one year. Whether that appeases France's angry mob is another matter.

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Assessing quantitative easing

Muzzled

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Politics stops the Fed from expanding an asset-purchase scheme

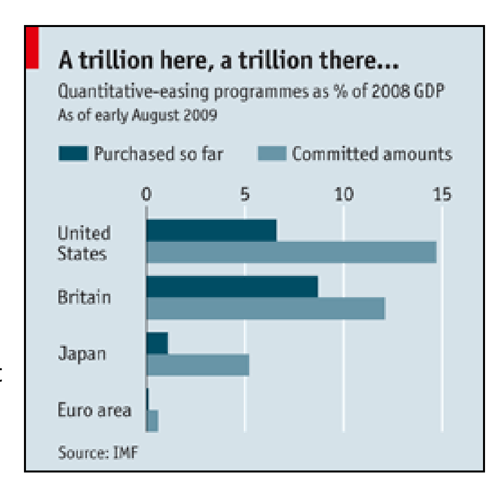
BACK IN 2002, before he became chairman of the Federal Reserve, Ben Bernanke claimed that if short-term interest rates fell to zero, a central bank still had the ultimate weapon: printing money by purchasing government bonds. Having now actually tried quantitative easing himself, Mr Bernanke is discovering its limits.

In March the Fed announced plans to purchase $300 billion of Treasury debt by September with newly printed money (to be more precise, electronic money in the form of bank reserves) and to more than double planned purchases of mortgage-related debt to $1.45 trillion. The $300 billion in Treasury purchases, in particular, were widely assumed to be the start of a much more substantive plan. Yet the Fed's latest policy meeting wrapped up on August 12th without any plans to expand either scheme, although it did move the completion date for Treasury purchases back to the end of October and kept the option of boosting purchases later. It left its short-term interest-rate target at zero to 0.25%. Such inaction contrasts with the Bank of England's decision on August 6th to expand its programme of asset purchases, mainly of government bonds, from £125 billion ($206 billion) to £175 billion.

Comparisons are inexact. The Fed has been intervening more aggressively than the bank in other ways. The programmes also have different rationales. The Fed emphasises the ability of bond purchases to lower yields and improve liquidity in private debt markets. The Bank of England says its programme aims to boost spending by putting more money into the economy.

Analysing the programmes' precise impacts is also tricky. Government-bond yields in both Britain and America initially fell sharply on the announcement of the asset-purchase programmes, which are substantial relative to GDP (see chart). Yields have since retraced that drop in Britain and bounced higher than before in America. But lots of factors are at play. Expected inflation (as implied by the gap between conventional and inflation-indexed bond yields) has risen. The fear of global meltdown that drove investors to the safety of governments bonds has ebbed. Nevertheless, an IMF study estimates that Britain's longer-term yields are 40-100 basis points lower than they would have been without the bank's purchases.

The impact on private yields is also probably positive. Macroeconomic Advisers, a consultancy, estimates that American mortgage rates are a percentage point lower relative to Treasuries as a result of the Fed's asset purchases. The Bank of England takes some credit for a narrowing in corporate-bond spreads. The European Central Bank says the announcement of plans to buy €60 billion ($85 billion) of covered bonds has helped revive new issuance and bring down spreads.



If the programmes are doing some good, why is the Fed not expanding them? The outlook has improved, for one thing: America's economy is levelling out, it noted on August 12th. But the main reason is political, not economic. The Fed's Treasury-purchase plan prompted charges that it was inviting hyperinflation and had subordinated itself to the government's deficit needs. Alan Greenspan, a former Fed chairman, says inflation will exceed 10% if the Fed fails to shrink its balance-sheet and raise rates, and 3% for a time even if it does.

Needless to say, that is not the Fed's view: it still foresees rising unemployment and falling inflation. But many officials have concluded that, for now, the benefits of buying more Treasuries do not outweigh the costs of a damaging rise in inflation expectations and a perceived loss of independence. Even the ultimate weapon is useless if you are too nervous to use it.

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Buttonwood

Law of easy money

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From The Economist print edition

A 300-year-old example of quantitative easing

Illustration by S. Kambayashi



"IF FIVE hundred millions of paper had been of such advantage, five hundred millions additional would be of still greater advantage." So Charles Mackay, author of *Extraordinary Popular Delusions and the Madness of Crowds*, described the "quantitative easing" tactics of the French regent and his economic adviser, John Law, at the time of the Mississippi bubble in the early 18th century. The Mississippi scheme was a precursor of modern attempts to reflate the economy with unorthodox monetary policies. It is hard not to be struck by parallels with recent events.

Law was a brilliant mathematician who used his understanding of probability to help his gambling habit. Escaping from his native Scotland after killing a rival in a duel, he made friends with the Duke of Orleans, the regent of the young king Louis XV.

The finances of the French government were in a terrible mess. Louis XIV had spent much of his long reign fighting expensive wars. Tax collection was in the hands of various agents, who were more concerned with enriching themselves than the state. Not only was the monarchy struggling to pay the interest on its debt, there was also a credit crunch in the form of a shortage of the gold and silver coins needed to fund economic activity.

Law's insight was that economic activity could be boosted by the use of paper money that was not backed by gold and silver. He was well ahead of his time.

Establishing confidence in a new monetary system was the trickiest part. Law had the benefit of working for an absolute monarchy which could decree that taxes should be paid in the form of notes issued by his new bank, Banque Générale. He also believed, having observed the success of the Dutch in exploiting the spice trade in the East Indies, that France could use paper money to develop its colonial possessions. Hence the Mississippi scheme, under which Law created the Compagnie d'Occident to exploit trade opportunities in what is now the United States. The money raised from these share issues was used to repay the government's debts; on occasion, Law's bank lent investors the money to buy shares.

Turn this into modern economic jargon and Law could be described as creating a stimulus package for French economic activity. But rather than rescuing sunset industries such as carmaking, Law was an early venture capitalist, financing the dynamic potential of the Mississippi delta.

The problem was that the delta was a mosquito-infested swamp. According to Niall Ferguson, a historian, 80% of the early colonists died from starvation or disease. Even though the company had monopolies over things like tobacco, it had little chance of generating enough income to fund the dividends Law had promised.

So a vicious circle was created, in which a growing money supply was needed to bolster the share price of the Mississippi company and a rising share price was needed to maintain confidence in the system of paper money. You can see parallels with recent times, in which money was lent on the back of rising asset prices, and higher prices gave banks the confidence to lend more money.

When the scheme faltered Law resorted to a number of rescue packages, many of which have their echoes 300 years later. One was for the bank to guarantee to buy shares in the Mississippi company at a set price (think of the various government asset-purchase schemes today). Then the company took over the bank (a rescue along the lines of Fannie Mae and Freddie Mac). Finally there were restrictions on the amount of gold and silver that could be owned (something America tried in the 1930s).

All these rules failed and the scheme collapsed. Law was exiled and died in poverty. The French state's finances stayed weak, helping trigger the 1789 revolution. The idea of a "fiat" currency was perceived to be the essence of recklessness for another two centuries and the link between money and gold was not fully abandoned until the 1970s, when the Bretton Woods system expired.

Of course, the parallels with today are not exact. Law's system took just four years to collapse; today's fiat money regime has been running for nearly 40 years. The growth in money supply has been less excessive this time. Technological change and the entry of China into the world economy have generated growth rates beyond the dreams of 18th-century man. But one lesson from Law's sorry tale endures: attempts to maintain asset prices above their fundamental value are eventually doomed to failure.

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The Madoff affair

A sidekick sings

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Frank DiPascali will help prosecutors understand the Madoff fraud

HOW did Bernie do it? With an old IBM computer, oodles of chutzpah and, it seems, help from multiple sidekicks. On August 11th Frank DiPascali, the senior lieutenant in Bernard Madoff's bogus fund-management business, admitted to fraud and was arrested. His willingness to confess and, apparently, to co-operate—in contrast to Mr Madoff, who went to jail insisting he acted alone—is a coup for prosecutors. They will waste no time going after the unidentified "other people" with whom Mr DiPascali says he and his boss perpetrated the scam.

Mr DiPascali was the main point of contact for investors, who ranged from Jewish charities to film moguls. He also oversaw the mechanics of the vast Ponzi scheme. It purported to be making steady, double-digit returns trading options on a share index. In fact, client funds sat in an account at JPMorgan and were withdrawn only to meet redemptions or to be parked in Treasuries and the like. This was "nothing more than a slush fund", according to a complaint against Mr DiPascali by the Securities and Exchange Commission.

Though there was no actual trading, the conspirators were far from idle. They cooked up phantom trading records, client confirmations and account statements to corroborate the fictitious investment strategy. They made thousands of wire transfers between the firm's London and New York offices to make it look like it was earning commissions from real transactions.

Hindsight is a wonderful thing when cooking the books. The complaint says that Mr DiPascali "picked advantageous historical prices, often near the lows, to create the appearance of a profit once the purported trade was booked." A single computer was programmed to allocate trades, pro rata, to individual accounts.

Some of the ruses bordered on comical. Worried that returns were suspiciously high, Mr Madoff occasionally instructed Mr DiPascali to book fake trades designed to lose money. They even created a fake computer platform so that, should outsiders spring a surprise visit, they could be shown "real-time" trading.

Absurd, perhaps, but not amateurish. The two made full use of their deep understanding of the workings and oversight of stockmarkets to pull the wool over inspectors' eyes. They created a list of counterparties that were unlikely to be checked on: European firms for American regulators, and vice versa. They pretended to exit their options-trading strategy and shift into Treasuries before the end of each quarter, to avoid having their fishy positions disclosed in investors' filings. To hide the scale of the operation, which had thousands of accounts, they devised a subset of 10-25 "special" accounts, which they presented as their full universe of business. Why regulators swallowed this, when Mr Madoff was widely known to have had hundreds of clients, is a mystery.

Who else was involved? Prosecutors have filed charges against the firm's accountant, who denies them. They are looking to build cases against certain investors and "feeder" funds that funnelled their money to Mr Madoff. But the most fertile territory could be the co-workers whose help would have been needed to handle the programming and the mounds of paperwork. In court, Mr DiPascali lamented becoming "loyal to a terrible, terrible fault". In that, he was surely not alone.

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Retail bonds in Europe

Small fry wanted

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European companies court individual bond investors

AFTER raising nearly €8 billion ($11.2 billion) in a rights issue in June, Enel was not expected to make a quick return to the markets. But on July 31st the Italian utility approved plans for bond issues worth up to €10 billion. Given "huge interest" in corporate bonds, the company should cast for more credit whenever it can, says Luigi Ferraris, Enel's finance chief.



Much of that interest comes from individuals. Enel's proposed issues will target both institutional and retail investors. The retail appetite for corporate bonds has been a fillip for other cash-strapped European borrowers. In June when Eni, an Italian energy group, sought to raise €1 billion from retail investors, it attracted almost €6 billion in orders. EDF, a French utility, raised more than €3 billion from a similar retail-focused issue. In the first six months of 2009 the number of corporate issues raising more than €1 billion in denominations of €1,000 or less surpassed recent full-year totals (see chart).

Borrowers are normally hesitant to offer bonds in denominations below €50,000, the level at which onerous EU reporting requirements kick in. Marketing bonds to thousands of individuals instead of a handful of institutions is costlier. Bankruptcy is more complex. But the benefits of tapping new sources of credit now appear to outweigh the costs. And with cash parked in bank accounts earning little interest, savers are hungry for higher returns. The practice may even spread to Britain, where issuers have been warier of retail investors. The London Stock Exchange, owner of a thriving retail-bond exchange in Italy, has mooted plans for a similar platform on its home soil.

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Rebalancing the world economy: Japan

Stuck in neutral

Aug 13th 2009 | TOKYO
From The Economist print edition

Japan's long-standing inability to rebalance its economy is bad for the world and even worse for its own people. The last in our series

Alamy



NO CITIZENS in the rich world take as few holidays as the Japanese. No wonder. This week, as millions left the cities for an annual pilgrimage to villages where they venerate the souls of their ancestors, many were likely to be stuck in 40-mile traffic jams on oven-like expressways, cursing the midsummer heat.

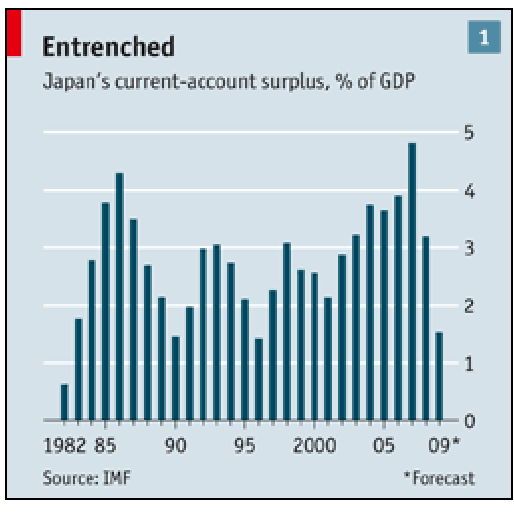
Such misery is common during the Buddhist festival of Obon, but it is worse this year. One of the government's aggressive measures to alleviate the economic crisis is to encourage people to spend money on hotels, transport cafés and other forms of leisure. To do that, it has slashed the cost of toll roads to almost one-tenth of their normal level, attracting yet more people on to fume-choked roads.

This is not the first time Japan's leaders have tried to emphasise the fun side of life to strengthen Japan's domestic economy and leave it less vulnerable to the vagaries of world trade. In 1986, when Japan's bulging current-account surplus was a huge source of tension with America, the Maekawa report, written by a panel of Japanese experts, preached the virtues of more time off as a means for workaholics to let their hair down and spend, spend, spend.

It never happened. Instead, what Japan gave the world in the late 1980s was a lesson in how tricky it is to rebalance economies. The country first mollified America and evened out its trade books by raising the value of the yen. But as the dollar slid, it reversed course and cut interest rates, which boosted spending on everything from golf-club memberships at home to splashy buildings in Manhattan. Cheaper credit had the effect of stoking the vast stockmarket and land bubble that popped with disastrous consequences in the 1990s and beyond.

Fast forward to this decade and Japan's current-account surplus was higher than ever, reaching a record 4.8% of GDP in 2007 (see chart 1). That is because the impact of foreign trade on the growth of the economy is still much larger than in many other, more open economies. Export growth increased from 4% a year in the decade beginning in 1992 to nearly 10% annually from 2002-07. OECD figures show that the contribution of foreign trade to GDP growth during those years was as high in Japan as in Germany. Some of the bumper profits of large exporters selling Lexus cars, video-game consoles and flat-screen TVs to Westerners during the cheap-credit era were also pumped back into building factories and investing in new technology at home, which further boosted growth. According to OECD estimates, export industries generated about a third of annual output during the pre-crisis years.

A current-account surplus that has persisted for almost all of the past three decades, whether the yen was strong or weak, suggests a structural issue rather than a cyclical one. A recent report on Asian imbalances by Morgan Stanley shows that throughout the boom-and-bust periods since the early 1980s, investment has consistently fallen short of savings (see chart 2). Households, which used to be Japan's greatest hoarders, put less aside in the years before the financial crisis as a combination of low wage-growth and an ageing population took its toll: the household-saving rate fell from above 10% in the 1990s to about 2.2% in 2007. But the country continued to spend less than it earned because exporters squirrelled a chunk of their profits away.



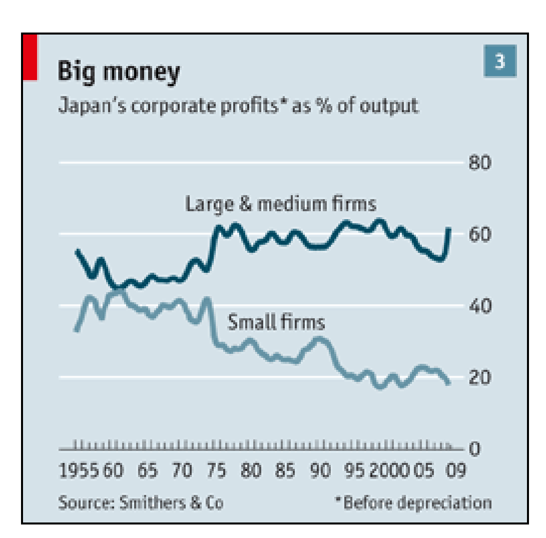
A combination of factors kept domestic demand below par. Japanese workers benefited less from the recent export boom than they had previously: the OECD says their share of GDP fell from a peak of 73% in 1999 to 65% in 2007. Japan's ugly demography, with a shrinking working-age population and a growing grey-haired one, helped the downward pressure on wages. More high-paid workers were retiring and being replaced by lower-paid youngsters, which dragged down overall wages. The retirees did not spend as freely as they might because of uncertainty over the government's commitment to state pensions.



Two other features in the economy also held down pay, and hence consumer spending. First, Japan suffers from a glaring gap between large firms, which are highly profitable, and small ones. According to the IMF the latter continue to struggle with the legacy of Japan's 1990s debt crisis. Although they provide about 70% of jobs in Japan, they have meagre profits from which to fund wage increases (see chart 3).

Second, within the manufacturing industry, there is a big disparity between unionised workers, who enjoy high pay, bonuses and job security, and "non-regular" workers. In the years before the crisis the latter grew to account for about one-third of the workforce, as firms sought to increase flexibility in the face of competition from low-wage rivals in Asia. That shift led wages to fall in 2007, even though the economy was near full employment. These wage pressures meant that the country's five-year growth spurt before the crisis—the longest in Japan's post-war history—had very little impact on the average household. Over the five years to 2007 real private consumption grew by 1.1% a year, about the same level as during the "lost decade" of the 1990s. That was higher than in Germany, but far lower than in America, where consumer spending grew almost three times as fast.

Skew etiquette



Why is Japan such a lopsided economy? Explanations for why the Japanese are serial exporters include government support of trade and industry (the links between big business, the ruling party and civil servants are known as the "iron triangle"), a strong sense of shared mission among firms' employees, and an obsession with detail that enables Japan to manufacture high-quality goods.

The aversion to spending is also deep-rooted. Richard Koo, chief economist at the Nomura Research Institute, believes that domestic demand is stunted by a respect for hard work, which chains people to their desks rather than unleashing them to enjoy themselves in shops or on holiday. A further structural problem is the way the Japanese save in order to rebuild their homes every

15 years or so. This is a legacy of centuries of earthquakes and fires in Japan, but it prevents an American-style culture of lavish home improvements.

There is also a reluctance to borrow. Consumers rarely shift credit-card debts from one card to another. Small businesses are still paying off loans from the previous crisis; banks are shy of lending because of the current one. Katsuyuki Hasegawa, chief market economist at Mizuho Research Institute, says the anti-debt culture is deeply entrenched. "People don't like borrowing. They just like paying back."

The crisis that has hit Japan since 2008, and which is expected to generate a decline of at least 5% of GDP this year, is only likely to make people more cautious. The export collapse that first hit Toyota and other big carmakers quickly spread down the supply chain to the domestic economy. As profits dived, so did business investment. Unemployment jumped from 3.8% in October to 5.4% in June—not as high as in America and Europe, admittedly, but accompanied nonetheless by yet another onslaught on wages. In this context the sharp narrowing of the current-account surplus to 1.4% of GDP in the first quarter is nothing to celebrate.

In the short term Japan's path out of the crisis is familiar. The government has stepped in with one of the most aggressive fiscal-stimulus packages in the rich world. Hopes are pinned on a pick-up in exports to China as it rebounds. On August 17th Japan is expected to report its first increase in quarterly GDP in five quarters.

But in the long term, rebalancing the economy is the best way to ensure higher growth. This is particularly important to Japan because it is saddled with the highest public-debt-to-GDP ratio in the rich world, at about 180%, the legacy of years of propping up a moribund economy.

The debt will rise even higher as spending on the elderly increases, raising the possibility of a fiscal crisis if ever the Japanese grow tired of funding their government's borrowing habit. (So far Japanese bond yields have risen less than in other crisis-hit countries such as America and Britain, partly because most of the debt is held at home, but the IMF warns that Japan would be very vulnerable if there were a loss of confidence in the sustainability of public debt.)

Eventually taxes will have to rise to reduce these debts. But the best way to ensure that does not throw the economy into another slump is to foster a more even-keeled recovery, with services playing a bigger part. Such businesses—retailers, builders, hairdressers and the like—are so inefficient that, according to the OECD, they have dragged down labour-productivity growth in the country as a whole from 4% in the boom years of 1976-89 to just 2% between 1999 and 2004. Only brothels appear to be doing well. A recent report from the Bank of Japan showed their numbers have mushroomed in the otherwise depressed northern city of Sapporo. Nearby eateries, by contrast, have shut down in droves.

The OECD last year set out to explain why service industries were so poor in Japan. Research and development (R&D) in services was minuscule—one-quarter the level of America, as a share of total R&D. Competition among firms is stifled, with very high levels of concentration and high barriers to new entrants. Information technology in services is poor, an extraordinary weakness in such a tech-savvy country. Multinationals, meanwhile, find it unusually difficult to set up Japanese affiliates in fields such as telecoms and travel because of investment restrictions and regulatory barriers. But the outsiders' record, by and large, should encourage Japan to deregulate further: the OECD found that productivity growth among those foreign firms that did enter the market was 1.8 times the national average.

With the working-age population likely to shrink by 9% during the next decade, according to government estimates, the quest for higher productivity will become pressing. That search has costs of its own: restructuring would require job losses in some enterprises. But an unshackled service industry would eventually generate wage gains. Without one, overall living standards will suffer.

One of the most sensible ways to achieve higher productivity would be to slash the forest of regulations that surround service industries, protecting them from competition in the name of quality control. Farming could be liberalised, as could heavily protected bits of the economy such as energy, transport, health care and education. Policies to encourage investment, both foreign and domestic, would help.

Vote sinners

But in the run-up to general elections on August 30th, a poll that may mark the end of 54 years of almost unbroken rule by the Liberal Democratic Party, there is little talk of rebalancing the economy. Instead,

politicians still seem fixated by exports, this time geared towards fast-expanding but lower-margin regions such as China rather than America. There is also talk of re-regulating wages by restricting the hiring of non-regular workers in manufacturing.

None of the election rhetoric sounds enough to jump-start the juggernaut that Japan, still the world’s second-largest economy, could be. Nor does it offer Japanese people much cause for optimism that the daily grind of hard work and modest pay will get any better. Despite the traffic jams, spending a few of their seven days’ annual holiday venerating the past is more fun than contemplating the future.

Video: See Japan’s structural imbalances at Economist.com/videographics

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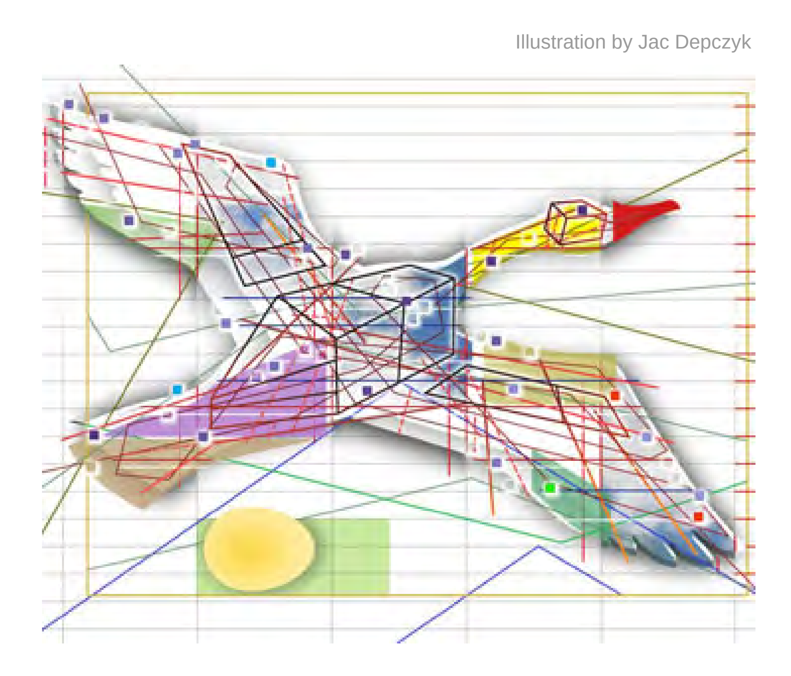
Economics focus

Cause and defect

Aug 13th 2009
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Instrumental variables help to isolate causal relationships. But they can be taken too far

Illustration by Jac Depczyk



"LIKE elaborately plumed birds…we preen and strut and display our t-values." That was Edward Leamer's uncharitable description of his profession in 1983. Mr Leamer, an economist at the University of California in Los Angeles, was frustrated by empirical economists' emphasis on measures of correlation over underlying questions of cause and effect, such as whether people who spend more years in school go on to earn more in later life. Hardly anyone, he wrote gloomily, "takes anyone else's data analyses seriously". To make his point, Mr Leamer showed how different (but apparently reasonable) choices about which variables to include in an analysis of the effect of capital punishment on murder rates could lead to the conclusion that the death penalty led to more murders, fewer murders, or had no effect at all.

In the years since, economists have focused much more explicitly on improving the analysis of cause and effect, giving rise to what Guido Imbens of Harvard University calls "the causal literature". The techniques at the heart of this literature—in particular, the use of so-called "instrumental variables"—have yielded insights into everything from the link between abortion and crime to the economic return from education. But these methods are themselves now coming under attack.

Instrumental variables have become popular in part because they allow economists to deal with one of the main obstacles to the accurate estimation of causal effects—the impossibility of controlling for every last influence. Mr Leamer's work on capital punishment demonstrated that the choice of controls matters hugely. Putting too many variables into a model ends up degrading the results. Worst of all, some relevant variables may simply not be observable. For example, the time someone stays in school is probably influenced by his innate scholastic ability, but this is very hard to measure. Leaving such variables out can easily lead econometricians astray. What is more, the direction of causation is not always clear. Working out whether deploying more policemen reduces crime, for example, is confused by the fact that more policemen are allocated to areas with higher crime rates.

Instrumental variables are helpful in all these situations. Often derived from a quirk in the environment or in public policy, they affect the outcome (a person's earnings, say, to return to the original example) only through their influence on the input variable (in this case, the number of years of schooling) while at the same time being uncorrelated with what is left out (scholastic ability). The job of instrumental variables is to ensure that the omission of factors from an analysis—in this example, the impact of scholastic ability on the amount of schooling—does not end up producing inaccurate results.

In an influential early example of this sort of study, Joshua Angrist of the Massachusetts Institute of Technology (MIT) and Alan Krueger of Princeton University used America's education laws to create an instrumental variable based on years of schooling. These laws mean that children born earlier in the year are older when they start school than those born later in the year, which means they have received less schooling by the time they reach the legal leaving-age. Since a child's birth date is unrelated to intrinsic ability, it is a good instrument for teasing out schooling's true effect on wages. Over time, uses of such instrumental variables have become a standard part of economists' set of tools. *Freakonomics*, the 2005 bestseller by Steven Levitt and Stephen Dubner, provides a popular treatment of many of the techniques. Mr Levitt's analysis of crime during American election cycles, when police numbers rise for reasons unconnected to crime rates, is a celebrated example of an instrumental variable.

Two recent papers—one by James Heckman of Chicago University and Sergio Urzua of Northwestern University, and another by Angus Deaton of Princeton—are sharply critical of this approach. The authors argue that the causal effects that instrumental strategies identify are uninteresting because such techniques often give answers to narrow questions. The results from the quarter-of-birth study, for example, do not say much about the returns from education for college graduates, whose choices were unlikely to have been affected by when they were legally eligible to drop out of school. According to Mr Deaton, using such instruments to estimate causal parameters is like choosing to let light "fall where it may, and then proclaim[ing] that whatever it illuminates is what we were looking for all along."

IV leagues

This is too harsh. It is no doubt possible to use instrumental variables to estimate effects on uninteresting subgroups of the population. But the quarter-of-birth study, for example, shone light on something that was both interesting and significant. The instrumental variable in this instance allows a clear, credible estimate of the return from extra schooling for those most inclined to drop out from school early. These are precisely the people whom a policy that sought to prolong the amount of education would target. Proponents of instrumental variables also argue that accurate answers to narrower questions are more useful than unreliable answers to wider questions.

A more legitimate fear is that important questions for which no good instrumental variables can be found are getting short shrift because of economists' obsession with solving statistical problems. Mr Deaton says that instrumental variables encourage economists to avoid "thinking about how and why things work". Striking a balance between accuracy of result and importance of issue is tricky. If economists end up going too far in emphasising accuracy, they may succeed in taking "the con out of econometrics", as Mr Leamer urged them to—only to leave more pressing questions on the shelf.

Links to the papers referred to in this article can be found here

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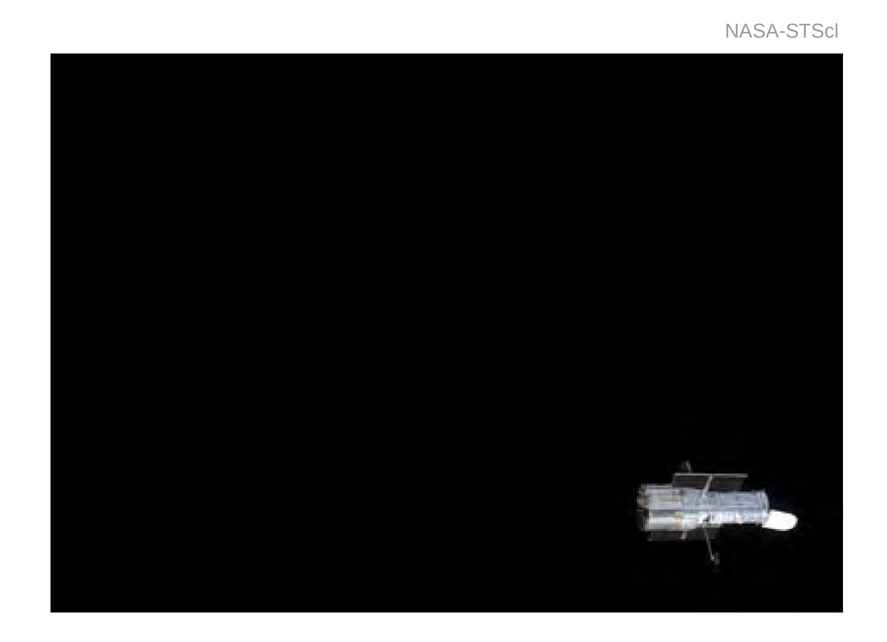
The future of astronomy

Black-sky thinking

Aug 13th 2009 | RIO DE JANEIRO
From The Economist print edition

The first of four articles from the International Astronomical Union meeting looks at a battle between Big Science and human hunches

NASA-STScI



SINCE time immemorial man has looked at the stars in awe and wonderment. No longer. The observatories where light is collected are now run by robots that neither dirty the instruments nor take night-time naps. Does it matter? Some of the astronomers at this year's meeting of the International Astronomical Union (IAU), held in Rio de Janeiro from August 3rd to 14th, think it does. They discussed what could be done to halt their subject's trend towards mining data gathered by computers rather than peering into telescopes.

The Rio meeting is the high point of what has been dubbed by the union as the International Year of Astronomy. The reason for picking 2009 to receive this honour is that it is exactly 400 years since Galileo Galilei turned his telescope on the heavens to study what the naked eye could not disclose, and also since Johannes Kepler revealed to the world that planetary orbits are ellipses, not circles. These two events can be seen, in retrospect, as the beginning of modern astronomy.

The pace of discovery has not slowed down. Indeed, more than one participant in the meeting described the present as a "golden age". The rate of discoveries has been increasing, along with the means to keep up with the details. That has, in turn, led to bigger and more expensive telescopes, and the introduction of management techniques intended to ensure the smooth running of large projects. But it is that managerialism that is beginning to worry some of the more thoughtful members of the union. They fear that although it brings short-term benefits, it may, in the long run, crush individual flair.

Simon White of the Max Planck Institute for Astrophysics in Garching, Germany, is one such worrier. He observes that in the 19th century and for most of the 20th, too, scientific progress usually came from brilliant individuals formulating and testing hypotheses using data accumulated by relatively modest means.

Big science has its place, of course. For one thing, enormous amounts of data allow subtle effects to be detected statistically. But Dr White suggests astronomers should ensure small science can flourish alongside its larger counterpart by, for example, ensuring that telescopes designed to look for big fish can also be used for projects that might be considered as small fry.

Thinking space

Another way to encourage gifted individuals might be to reform the way time on telescopes is allocated. The IAU's new president, Robert Williams of the Space Telescope Science Institute in Baltimore, Maryland, is a supporter of this idea. He reckons decisions about who gets what observing time should be made by the directors of observatories, answerable to a governing body, rather than by groups of the great and good, as tends to happen now.

"High-risk, high-reward projects require hard decisions that are best made by individuals, not committees," he says. And he should know. As director of the Space Telescope Science Institute he was, in 1995, allocated ten days on *Hubble* (pictured above), America's most famous eye in the sky. Instead of using that time on a project with a preordained objective, he asked, in what might be seen as an act of either modesty or bravura, that the telescope be pointed at a typical patch of sky and left there for the whole period, to see what it could see.

The result was the Hubble Deep Field, a fantastically detailed image of a small region in a constellation called Ursa Major. The field of view is so narrow that only about 20 stars from the Milky Way, the galaxy in which the Earth resides, lie within it. What it shows instead is almost 3,000 galaxies, some of which are the most distant (and hence the youngest) ever observed. The image demonstrates that the universe is, indeed, uniform over large scales and that the Earth occupies a typical region of it. It is unlikely that a committee would have had the guts to allocate so much time to what was a speculative punt.

Yet despite the professed desire of some to do so, astronomers cannot turn their backs on big science. In particular, to see faint, distant objects at the dawn of time, as Dr Williams did with *Hubble*, you need to collect a lot of light. That means your telescopes need big mirrors. And big mirrors do not come cheap.

Back on Earth, the biggest mirrors in prospect belong to three telescopic projects that will, by coincidence, all come to fruition in 2018, if their backers get their way. The Giant Magellan Telescope, a joint effort by America, Australia and South Korea that is to be built in the Atacama Desert in Chile, would have seven mirrors, each 8.4 metres across, giving an effective diameter of 25 metres. An even larger beast, dubbed the Thirty Metre Telescope, for obvious reasons, is a collaboration between American and Canadian universities. It has been on the drawing board since 1990. Last month its project board announced that, if funding were forthcoming, it would be built on Mauna Kea in Hawaii.

Science Photo Library



Galileo moved the Earth

The third, the European Extremely Large Telescope, is the suggested replacement for the Overwhelmingly Large Telescope, a proposal rejected by the European Southern Observatory three years ago when it discovered that the bill would also be overwhelmingly large. Its mirror would be 42 metres across, and it would probably be built either on one of the Canary Islands or in Chile.

Besides these new conventional telescopes, completely novel ways of doing Big Astronomy are likely to emerge to tempt astronomers back into its clutches. Several projects are already under way to detect gravitational waves—ripples in the fabric of spacetime itself—although none has yet caught its quarry. Should they, or their successors, eventually do so, it would open up a new window on the universe, allowing astronomers to study massive objects such as colliding black holes in unprecedented detail.

Astrophysicists have also begun to be able to detect the directions from which streams of subatomic particles called neutrinos arrive, and progress is being made as well on interpreting cosmic rays. Once these are better understood, astronomers could use them to study the universe in the way they now use light and radio waves.

Yet astronomers are still right to want space for the small. The two most exciting recent findings—the discovery of "dark energy", which pushes space itself apart, and of planets beyond the solar system—were made using modest equipment. It is the very success of the small that promotes the growth of the big.

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Galaxies in the early universe

Rocking the cradle

Aug 13th 2009 | RIO DE JANEIRO
From The Economist print edition

The discovery of some massive infants forces a rethink of galactic evolution

IN THE crazy world of Dr Seuss, an American children's author, a bird called a Pelf lays eggs that are three times as big as herself. At this week's meeting of the International Astronomical Union, astronomers were asked to entertain equally odd thoughts when they were presented with the latest evidence that some early galaxies, although smaller than their more recent counterparts, contain much more mass. It is like being handed a baby that weighs three times as much as its mother.

The objects in question are "red compact" galaxies, in particular a well-studied one called 1255-0 that formed just 3 billion years after the Big Bang. As the universe is thought to be 13.7 billion years old, the light reaching Earth from this galaxy shows what it was like some 10.7 billion years ago, when it was the equivalent of a newborn. Images suggest that the galaxy is 3,000 light years across—just a fifth of the size of the Earth's home galaxy, the Milky Way—but about four times as massive.

To check how compact 1255-0 really was, a group of astronomers led by Pieter van Dokkum of Yale University analysed the speed at which its stars were moving. The researchers reasoned that if it really was as small and as massive as it appeared, those stars would be whizzing round its centre at high velocity.

They were able to calculate the speed of the stars in question using the Doppler effect—the change in frequency, and thus in colour, that a light wave undergoes according to whether the thing that emitted it is moving towards or away from the observer. (The changing pitch of an ambulance siren is the equivalent effect for sound.) The Doppler shifts of the light from different parts of 1255-0 showed Dr van Dokkum and his colleagues that the average orbital velocity of this galaxy's stars was 510 kilometres a second, the highest value ever recorded. This suggests that previous estimates of its size and mass are right.

Growing and shrinking

Red compact galaxies are thought to evolve by growing into blob-shaped galaxies called ellipticals, which are common today, and there are also several of these near 1255-0. Although ellipticals are bigger than red compacts, they are usually less massive. That makes the process of transition from one to the other problematic. Mergers are ruled out. Though they would make the babies bigger, they would also make them heavier, rather than lighter. The shock involved would create new, younger stars as well, and these do not appear to be there.

One possibility discussed at the meeting is whether the distribution in space of dark matter might help explain what happens. It may be that the red compacts are heavy not because they contain more stars but because they contain more of this substance, whose nature remains unknown, but which can be detected by its gravitational effects, and which seems to be about six times as abundant as the familiar matter of atoms and molecules. Yet this explanation is not terribly satisfactory either. Existing observations suggest that dark matter was smoothly distributed around elliptical galaxies by some 8 billion or 9 billion years ago. If extra dark matter is what is making earlier galaxies particularly massive, then something must have happened to redistribute the stuff between 10 billion years ago (when it clumped together in baby galaxies) and 9 billion years ago (by which time it was no longer lumpy).

That something would have to have been strange indeed, though—possibly a shift in the value of a fundamental constant such as the speed of light—to have caused compact galaxies to inflate while losing weight. Dr Seuss's hero never did find out how the Pelf learned to pull off her egg-laying trick. Perhaps astronomers will have better luck.

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Detecting habitable new worlds

The next blue planet

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The race is on to discover a second Earth

IN 1995, when Michel Mayor of the University of Geneva detected the first exoplanet (a planet that orbits a star other than the sun) he started a race that has gained pace ever since. Some 360 such planets have now been detected, but none is exactly equivalent to the Earth.

The closest so far is Gliese 581c, which was discovered in 2007 by Dr Mayor's colleague, Stéphane Udry. It is both rocky and orbits its parent star at a distance where liquid water could reasonably be expected to exist. However, since its parent star is a red dwarf—a far smaller and fainter object than the sun—that orbit is, in fact, much smaller that the Earth's around the sun. That, in turn, suggests Gliese 581c is likely to be tidally locked to its orbital period, so that one side of the planet always faces the star and the other never does. Having half a planet in permanent daylight and the other half in permanent darkness does not sound like a good recipe for life.

As astronomers heard this week at the International Astronomical Union meeting in Rio, two new missions—a French one launched in December 2006 and an American one launched on March 6th—are in the process of trying to add to the list. Dr Mayor told the meeting that the French mission, *CoRoT*, has now found 80 exoplanets. It does so by watching for small diminutions in the amount of light from a star as the planet in question passes in front of it, a phenomenon known technically as a transit. The details of all but seven of these transiting planets are still unpublished, but Dr Mayor gave the meeting a preview.

The planets discovered so far by *CoRoT* typically have a mass that is less than 30 times that of Earth, making them likely to have a solid, rocky surface. But they also orbit their stars rapidly, typically taking two or three months, rather than a year, to do so. For those who hanker after extraterrestrial life that is a pity. Such rapid orbits mean the planets in question are close to their parent stars, and thus likely to be tidally locked.

Other news from *CoRoT* is better, though. Some 80% of the planets Dr Mayor has found have siblings. The existence of so many neighbours suggests that planetary systems tend to be stable, and stability is good for the evolution of life. Dr Mayor described a system he has seen that has five rocky planets in it. They have masses of 11, 14, 26, 27 and 76 times that of the Earth. He concluded his talk by saying, "I am really confident that we have an Earth-like planet coming in the next two years."

He and his team may, however, be pipped at the post. On August 6th America's space agency, NASA, announced that its *Kepler* planet-detector (named after the man who worked out the laws of planetary motion, as this article explains) is also behaving well. A paper published in *Science* by William Borucki of the NASA Ames Research Centre based in Moffett Field, California, and his colleagues showed that *Kepler*, which also uses the transit-detection technique, has confirmed the existence of a Jupiter-like planet discovered in 2007 and provided more precise details of that planet's mass and orbital period. And *Kepler*'s instruments are more sensitive than *CoRoT*'s, so it should be capable of finding Earth-sized planets more easily than its French cousin.

Yet such space probes are not the only way of searching for other Earths. As part of his efforts to find new worlds, Dr Mayor is using the HARPS spectrograph, which is based at the European Southern Observatory in La Silla, Chile. He and his colleagues are training HARPS on ten nearby, bright and quiet stars three times a night, for 15 minutes at a time, for 50 nights a year, for at least two years, in the hope of spotting a nearby Earth-sized planet. The device works by detecting the tiny wobble given to a parent star when a planet passes it by. The spectrograph has already found 16 planets.

Meanwhile, David Bennett of the University of Notre Dame in Indiana wants to use a technique called gravitational microlensing to spot planets that might be missed by other methods. He told the conference that his approach would pick up not only small rocky planets orbiting at great distances from their parent stars, but also planets that had been ejected from their orbits. The idea would be to stare at a distant star

and report instances when its light had been bent by the gravity of a planet passing in front of it. Such signals would be brief and rare, but they would also be strong and unmistakable. Sooner or later, then, an Earth-sized planet will turn up. How Earth-like it will be in other ways, remains to be seen.

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The history of science

Kepler's world

Aug 13th 2009 | RIO DE JANEIRO
From The Economist print edition

Celebrating the work of a neglected astronomer

Science Photo Library



Kepler moved it elliptically

MUCH has been made of the 400th anniversary this year of Galileo pointing a telescope at the moon and jotting down what he saw (even though this had previously been accomplished by an Englishman, Thomas Harriot, using a Dutch telescope). But 2009 is also the 400th anniversary of the publication by Johannes Kepler, a German mathematician and astronomer, of "Astronomia Nova". This was a treatise that contained an account of his discovery of how the planets move around the sun, correcting Copernicus's own more famous but incorrectly formulated description of the solar system and establishing the laws for planetary motion on which Isaac Newton based his work.

Four centuries ago the received wisdom was that of Aristotle, who asserted that the Earth was the centre of the universe, and that it was encircled by the spheres of the moon, the sun, the planets and the stars beyond them. Copernicus had noticed inconsistencies in this theory and had placed the sun at the centre, with the Earth and the other planets travelling around the sun.

Some six decades later when Kepler tackled the motion of Mars, he proposed a number of geometric models, checking his results against the position of the planet as recorded by his boss, Tycho Brahe, a Danish astronomer. Kepler repeatedly found that his model failed to predict the correct position of the planet. He altered it and, in so doing, created first egg-shaped "orbits" (he coined the term) and, finally, an ellipse with the sun placed at one focus. Kepler went on to show that an elliptical orbit is sufficient to explain the movement of the other planets and to devise the laws of planetary motion that Newton built on.

A.E.L. Davis, of Imperial College, London, this week told astronomers and historians at the International Astronomical Union meeting in Rio de Janeiro that it was the rotation of the sun, as seen by Galileo and Harriot as they watched sunspots moving across its surface, that provided Kepler with what he thought was one of the causes of the planetary motion that his laws described, although his reasoning would today be considered entirely wrong.

In 1609 astronomy and astrology were seen as intimately related; mathematics and natural philosophy, meanwhile, were quite separate areas of endeavour. Kepler, however, sought physical mechanisms to explain his mathematical result. He wanted to know how it could be that the planets orbited the sun. Once he learned that the sun rotated, he comforted himself with the thought that the sun's rays must somehow sweep the planets around it while a quasi magnetism accounted for the exact elliptical path. (Newton did not propose his theory of gravity for almost another 80 years.) As today's astronomers struggle to determine whether they can learn from the past, Kepler's tale provides a salutary reminder that only some explanations stand the test of time.

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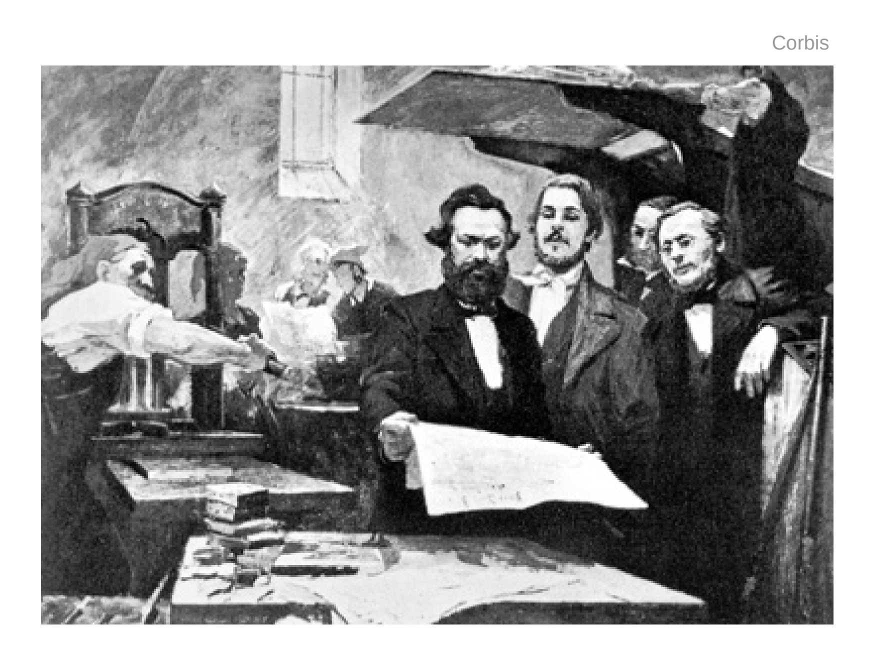
A biography of Friedrich Engels

A very special business angel

Aug 13th 2009
From The Economist print edition

The self-effacing friend who enabled "Das Kapital" to be written

Corbis



Marx's General: The Revolutionary Life of Friedrich Engels. By Tristram Hunt. *Metropolitan Books; 448 pages; $32. Published in Britain as "The Frock-Coated Communist: The Revolutionary Life of Friedrich Engels". Allen Lane; £25.* Buy from Amazon.com, Amazon.co.uk

WHEN the financial crisis took off last autumn, Karl Marx's "Das Kapital", originally published in 1867, whooshed up bestseller lists. The first book to describe the relentless, all-consuming and global nature of capitalism had suddenly gained new meaning. But Marx had never really gone away, whereas Friedrich Engels—the man who worked hand in glove with him for most of his life and made a huge contribution to "Das Kapital"—is almost forgotten. A new biography by a British historian, Tristram Hunt, makes a good case for giving him greater credit.

The two men became friends in Paris in 1844 when both were in their mid-20s, and remained extremely close until Marx died in 1883. Both were Rhinelanders (our picture shows Engels standing behind Marx in the press room of *Rheinische Zeitung* which they edited jointly) but came from very different backgrounds: Marx's father was a Jewish lawyer turned Christian; Engels's a prosperous Protestant cotton-mill owner. Marx studied law, then philosophy; Engels, the black sheep of his family, was sent to work in the family business at 17. While doing his military service in 1841 in Berlin, he was exposed to the ferment of ideas swirling around the Prussian capital.

Next, he went to work for the Manchester branch of the family business, Ermen & Engels. Manchester's "cottonopolis" in the mid-19th century was a manufacturer's heaven and a working man's hell, and it provided an invaluable lesson for Engels: that economic factors were the basic cause of the clash between different classes of society. By 1845, when he was just 24, he had not only learnt how to be a successful capitalist; he had also written a coruscatingly anti-capitalist work, "The Condition of the Working Class in England", which charted the inhumanity of modern methods of production in minute detail.

Engels left Manchester to work with Marx on the "Communist Manifesto" and the two of them spent the late 1840s criss-crossing Europe to chase the continental revolutions of the time, ending up in England. Marx had started work on "Das Kapital", but there was a problem. He had by then acquired an aristocratic German wife, a clutch of small children and aspirations for a comfortable bourgeois lifestyle, but no means of support.

Engels (whose name resembles the word for "angel" in German) offered an astoundingly big-hearted solution: he would go back to Manchester to resume life in the detested family cotton business and provide Marx with the money he needed to write his world-changing treatise. For the next 20 years Engels worked grumpily away, handing over half his generous income to an ever more demanding Marx. He also collaborated intensively on the great work, contributing many ideas, practical examples from business and much-needed editorial attention. When at last volume I of "Das Kapital" was finished, he extricated himself from the business and moved to London to be near the Marx family, enjoying life as an *Economist*-reading rentier and intellectual.

Engels was an enigma. Gifted, energetic and fascinated by political ideas, he was nevertheless ready to play second fiddle to Marx. "Marx was a genius; we others were at best talented," he declared after his friend's death. Mr Hunt does a brilliant job of setting the two men's endeavours in the context of the political, social and philosophical currents at the time. It makes for a complex story that can be hard to follow but is well worth persevering with.

Tall and handsome, Engels had a taste not just for ideas but for the good life—wine, women, riding with the Cheshire hunt—and seems to have felt little sense of irony that all these things were paid for by the proletariat's back-breaking labour. His domestic life was much more unconventional than Marx's. He lived, on and off, with a semi-literate Irish working-class girl, Mary Burns; then, when she died, with her sister, Lizzy, whom he married only on her deathbed. He had no children, though he chivalrously took responsibility for a boy whom Marx had fathered with a housekeeper.

Engels's sacrifices continued after Marx's death. He not only carried on funding the Marx family and their various hangers-on, but also spent years pulling together the chaotic notes Marx left behind for volumes II and III of "Das Kapital". Inevitably there were lots of loose ends which Engels tied up as he saw fit, and sometimes the results were more revolutionary than the author may have intended. In volume III, where Marx discussed the tendency of companies' profitability to fall and noted that this might lead to the "shaking" of capitalist production, Engels substituted the word "collapse", opening up the text to much more radical interpretations by 20th-century Marxists.

When Engels died in 1895, he eschewed London's Highgate cemetery where his friend was laid to rest. Self-effacing to the last, he had his ashes scattered off England's coast at Eastbourne—the scene of happy holidays with the Marxes.

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Speaking out for the Uighurs

Breathing fire

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From The Economist print edition

Dragon Fighter: One Woman's Epic Struggle for Peace with China. By Rebiya Kadeer with Alexandra Cavelius. *Kales Press; 426 pages; $28.95 and £22.99*. Buy from Amazon.com, Amazon.co.uk

AP



Mother of all Uighurs

TENSE days followed last month's ethnic violence in Urumqi, the capital of China's western region of Xinjiang. Your reviewer had to dodge blockades and angry crowds of Han Chinese protesters to reach the neighbourhood in the south of the city where the Turkic-speaking Muslim Uighurs live. There he found the modest, dilapidated building that is still named for Rebiya Kadeer. Given all the scorn that has been heaped on the exiled Uighur activist in recent years—she has been branded a conspirator and a terrorist—it is amazing that the Chinese government has yet to find another name for the building.

As she recounts in her memoir "Dragon Fighter", Ms Kadeer, now aged 62, was at the height of her wealth and influence in 1992 when she threw open the doors of her new seven-storey trade centre and offered cut-rate stall rentals to 1,000 local merchants. Her own ethnic group knew her as the "Mother of all Uighurs". She was celebrated as the most astute and successful businesswoman in the nation, and was accorded high political office by China's Communist Party rulers who distrusted her but hoped to co-opt her.

But then she fell from official grace. In the late 1990s she was stripped of all her titles and much of her wealth, and spent almost six wretched years in prison until she was released in 2005 on medical parole and went to the United States. China has continued to denounce her and three of her 11 children are in prison or under house arrest. The campaign against her rose to fever pitch last month after nearly 200 people were killed in the fighting between the Uighurs, the Han Chinese and the police.

The Beijing regime was quick to blame Ms Kadeer for orchestrating the entire chain of events. She has denied this, proclaiming her commitment to non-violence. Though the government claims to have proof of its charges, it has yet to reveal anything very convincing.

But there is plenty in her book to bolster some of the regime's more general complaints about Ms Kadeer's motives and methods. Unlike the Dalai Lama, who campaigns for greater autonomy for Tibet but stops short of urging independence, Ms Kadeer lambasts the Chinese as the illegitimate occupiers of her land, and openly longs to see them gone. She also acknowledges that she sought her fortune only in order to use it in the service of that goal. In one confession that is bound to cheer her Chinese accusers, she admits that in 1978, outraged when policemen beat a Uighur teenager to death, she arranged to turn his funeral into a protest march, all the while taking care to hide her involvement.

Not much else in the book will endear it to Chinese officials—or to Chinese nationalists, for that matter. There is, for instance, a brief introduction by the Dalai Lama himself, plus sharp criticism of Mao Zedong as "one of the most despicable mass murderers of the twentieth century". But the heart of the book is its relentless litany of Chinese abuses and a direct rebuttal of China's official narrative about its troubled history with the Uighur people.

The Beijing regime claims an ancient stake in the land and insists the Uighurs have gained from its benevolent rule since the Communists took over in 1949, integrating the East Turkestan Republic into China. But this line is hard to square with Ms Kadeer's descriptions of Chinese brutality, mendacity and pettiness.

"Dragon Fighter" was originally published in German in 2007. Its publication in English is timely. The

prose, having gone from Uighur to German to English, is not graceful but neither does it distract from the power of Ms Kadeer's story—from child refugee, poor housewife, wealthy tycoon and high official to political prisoner and exiled campaigner.

In its response to last month's violence, China has shown little desire to change its approach to Xinjiang and the restless Uighurs. Ms Kadeer is visiting Australia so Chinese diplomats have mounted a ham-fisted campaign to pressure Australia's National Press Club and Melbourne's city council into cancelling her speeches and the screening of her film, "The 10 Conditions of Love", at the Melbourne International Film Festival. Rather than address the root causes of Uighur discontent, China continues to attack the messenger.

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Valuing stockmarkets

When the signals flash red

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Wall Street Revalued: Imperfect Markets and Inept Central Bankers. By Andrew Smithers. *John Wiley; 256 pages; $27.95 and £16.99*. Buy from Amazon.com, Amazon.co.uk

IN EARLY 2000, just as the dotcom bubble was at its height, two books appeared that argued the stockmarket was overvalued. One, "Irrational Exuberance", turned its author, Robert Shiller of Yale University, into something of a guru. The second, "Valuing Wall Street" received less attention but its insights were no less perceptive. One of its two authors, Andrew Smithers, a British economist, has now returned to the theme of stockmarket valuation. This time he expands his remit to argue that it is not only possible to ascertain a fair value for stockmarkets but that central banks should try to do so and adjust their policies accordingly.

That would once have been a very controversial assertion. It requires central bankers to second guess the markets, to assume that they know more about share price values than investors do. Markets were believed to be efficient, that is to reflect all publicly available information.

But the bursting of the dotcom bubble followed by the credit crunch have dented the notion of perfect markets governed by rational investors. Mr Smithers prefers the idea that markets are "imperfectly efficient", in other words, that they fluctuate around their fair value.

Having argued this, Mr Smithers has to demonstrate two things. The first is a reliable method for valuation, of which he says there are two. One is the replacement cost of a company's assets, the so-called "q" ratio. The other (which was also an important point in Mr Shiller's book) is the cyclically adjusted price-earnings ratio, which compares shares with the profits earned over the previous ten years. When bull markets have reached their heights (as in 1929 and 2000), these ratios have clearly indicated overvaluation. Mr Smithers makes his case convincingly, dismissing alternative indicators of valuation, such as the dividend yield, along the way.

But that still leaves Mr Smithers to deal with a tricky second point: if there is a reliable way of knowing when markets are overvalued, why haven't investors used it to make their fortunes? Moreover, investors armed with such information would presumably sell their shares before they reached their peaks, thereby preventing the extremes from being reached in the first place.

The answer to this conundrum, which is at the heart of efficient market theory, is that valuation is not a useful guide to stockmarket direction over the short term. On Wall Street there were five valuation peaks in the 20th century, or one every 20 years or so. Most investors simply do not have that kind of time horizon. Get market timing wrong and they may lose a fortune (or, if they are a professional fund manager, their clients will). The market can be irrational for longer than you can remain solvent, as the saying goes.

A job for the banks

Even so, Mr Smithers argues that central banks should use the valuation data to decide whether stockmarkets are over- extended. And they should look at house prices and the price of liquidity (defined as the interest spread on corporate bonds that is not attributable to the risk of default) as well. None of this is easy. But central banks already try to estimate the "output gap", the extent to which economic growth is above or below trend, when setting interest rates—and that's fiendishly difficult.

In the past central bankers have claimed that, rather than try to pop bubbles, they should clean up the mess after they have burst. But the cost of the recent financial crisis makes that policy hard to justify. If all the signals (including house prices and liquidity) are flashing red, then central banks should act. Their best tool might not be increases in interest rates but changes in the capital ratios of banks. By requiring

banks to hold more capital, the flow of lending would slow and the fuel for speculation would diminish.

Such a policy would not eliminate financial crises or recessions altogether. But as Mr Smithers rightly says, the aim of central banks should not be to avoid an occasional mild recession but a big downturn, such as the world has been suffering.

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Fiction from Haiti

Meanness of the heart

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From The Economist print edition

Love, Anger, Madness: A Haitian Trilogy. By Marie Vieux-Chauvet. *Modern Library; 379 pages; $27*. Buy from Amazon.com

Illustration by Daniel Pudles

WITHDRAWN just after it was published in France in 1968 following a government warning that it would endanger the author's family, Marie Vieux-Chauvet's Haitian trilogy, "Love, Anger, Madness", has been an underground classic ever since. Finally released in France in 2005, it is now available in English.

The book provides three views of life under an increasingly oppressive and unpredictable regime. In the first novella, "Love", Claire, the eldest of three upper-class sisters, is a fiercely independent and intelligent woman whose dark skin makes her less marriageable than her younger siblings with their "gold under the skin". Until she finally rebels, Claire is a virtual slave to her family, while secretly consumed by desire for her French brother-in-law. The middle-class family in "Anger" is torn apart when the 20-year-old heroine, Rose, is forced to sleep with a soldier to stop the regime from seizing their land. In "Madness" a poet steels himself for one final stand after his village is ravaged by militants and he is trapped without food.

The daughter of a Haitian senator and a Jewish émigrée from the Virgin Islands, Vieux-Chauvet, who died in 1973, was a member of Haiti's "occupation generation". She was born in 1916, a year after Woodrow Wilson launched the American invasion of Haiti that was to last 19 years—damaging a nation proud of being the first black republic in the Western hemisphere and the only one that could boast a successful slave revolt.

The occupation, and the years immediately following it, form the backdrop to the triptych. But it is also hard not to sense the growing power of François "Papa Doc" Duvalier, who proclaimed himself Haiti's president for life in 1964, and whose family and followers, the terrifying *tonton macoutes*, were consolidating their grip on the country even as Vieux-Chauvet was secretly writing her book in her bedroom.

Oppression—commercial, political, sexual—dominates Vieux-Chauvet's writing, as it does the work of Haiti's two other 20th-century literary masters, Jacques Roumain, who featured peasant heroes in his fiction, and Jacques Stephen Alexis, who portrayed the American occupation as rape. It would be easy to dismiss Vieux-Chauvet's book as an out-of-date protest against colonialism, were it not for two elements that give it an important contemporary resonance: a powerful and erotic consciousness ("I am 39 years old and still a virgin. The unenviable fate of most women in small Haitian towns," writes Claire) and a sharp and constant questioning about who really is the victim and who the torturer. "To defend himself, man refines the meanness of his heart," she observes. True of Haiti 40 years ago, still true of too many places today.

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Football and economics

Game for geeks

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Why England Lose: and Other Curious Football Phenomena Explained. By Simon Kuper and Stefan Szymanski. *HarperSport; 344 pages; £15.99*. Buy from Amazon.co.uk

ALL football fans—all sports fans, come to that—are obsessed with numbers. They might not admit it: who wants to be called a "statto" or a "geek" just for knowing, say, how many league goals Rickie Lambert scored for Bristol Rovers last season? (Since you ask: 29.) But they are chasing data all the time. Scrutiny of the league table; glances at the watch as the final whistle nears; nervous inquiries about the score: all are quests for numbers.

Yet data do not merely describe. Make them sweat a little, and they will reveal deeper truths about football (soccer, if you prefer). That is the claim of Simon Kuper, a columnist for the *Financial Times*, and Stefan Szymanski, an economist who specialises in sport. They combine their skills to entertaining and mostly convincing effect.

The authors skewer a few pieces of lazily received wisdom. One is that football is "big business". Hmm. The turnover of Manchester United is dwarfed by that of BBA Aviation, a British firm that not many readers may have heard of. Another is that fans are loyal die-hards. The authors calculate the average proportion of English fans who are sure to watch their club next season: about half. People move to other towns. They have families. They reward success and shun failure.

A third myth is that clubs cannot buy success. They can, so long as they spend on players' wages rather than on transfers. Almost 90% of the variation in the positions of leading English teams is explained by wage bills. Transfer fees contribute little. New managers hoping to make their mark often waste money. Stars of recent World Cups or European championships are overrated. So are older players. So, curiously, are Brazilians and blonds.

It is possible to play the market wisely, by treating players in a similar way to stocks and shares: buy them before their prime (early 20s is best) and sell them the moment another club offers more than you think they are worth. Olympique Lyonnais, champions of France every year from 2002 to 2008, worked this out. So, earlier, did Arsenal, whose manager, Arsène Wenger, is obsessed with statistics. He also has a master's degree in economics.

There is much else in the book, such as why staging big tournaments may make countries happy but not rich; and why provincial cities provide more than their fair share of Europe's champion clubs. Perhaps the best chapter (for football-obsessed economists, anyway) analyses penalty kicks as public exercises in non-co-operative game theory: the authors speculate that an economist's advice about Manchester United's goalkeeper might, with luck, have won Chelsea the European Champions League in 2008. The least convincing is an attempt to rank countries by their enthusiasm for football. Norway comes top, which may be right.

As for the title, why do England lose? The answer is that they don't lose all that often, despite a meagre tally of one World Cup, 43 years ago, and no European championships. In fact, the national team does a little better than you would expect, given the country's size, wealth and experience in international football. Fans hope for more. The data, alas, are against them.

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A history of classical music finally reaches paperback

A feast for musicians, students and casual concert-goers

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Oxford History of Western Music (five volumes). By Richard Taruskin. *Oxford University Press; 3,856 pages; $185 and £90*. Buy from Amazon.com, Amazon.co.uk

AKG



Different, but not better or worse

"THE feeble beginnings of whatever afterwards becomes great or eminent are interesting to mankind." So wrote Charles Burney in 1776, opening his history of music with a subtle apologia for the historian's method. Before Burney, treatises on music had been theoretical, intended for practical use or to elaborate the eternal laws of musical science. The new historical approach brought with it the advantage of a more nuanced conception of the art, better suited to a wider public. But as in other areas of 18th-century learning, history introduced an element of doubt: had there really been progress from ancient to modern times? Might today's music not be worse than it used to be?

That the ancients eventually won the argument may be gleaned from the fact that we live in an artistic age almost completely dominated by the dead. The modern historian's task is all the more delicate. It is also lengthier, as is clear from a comparison of Burney's history with its contemporary equivalent, Richard Taruskin's five-volume work. Since its initial publication at the end of 2004, Mr Taruskin's five-volume survey of 1,200 years of musical tradition has come in for many criticisms—selectivity, subjectivity, riding roughshod over contemporary intellectual orthodoxy—but prolixity and over-comprehensiveness have not been among them.

If the original publication of Mr Taruskin's history sent shock waves through the academic musical world, the present reissue of the set in paperback is, if anything, a more momentous event. For the work, marvellously awash with judicious reflection on the latest scholarship though it is, is not really aimed at professional scholars. Rather, its greatest value comes in bringing the fruits of advanced scholarship to a general readership through a compelling, easy-to-read narrative.

But the original price of the set ($750 or £350), together with an internal arrangement that made the acquisition of individual volumes impractical, put Mr Taruskin's efforts beyond the reach of those who might benefit from it the most. The new edition is not only much cheaper but its individual volumes are packaged in a way that allows them to be bought separately.

The book excels for three main reasons. First, as the author is keen to point out, this is genuine history. We are presented not with a miraculous chain of great composers producing timeless masterpieces from nowhere. Rather, musical works and stylistic movements are presented in context so that, for example, the origins of the dynamic, dramatic style of Mozart and Haydn are shown to lie in Italian *opera buffa* rather than in the architecturally static idiom of Bach and Handel.

Second, and despite the sense of flying through the terrain at breakneck speed, the level of detail remains high, with extended commentaries on individual works that show how they were originally conceived and understood. Third, and despite protestations to the contrary in his preface, Mr Taruskin's subjective preferences make themselves felt throughout the weighty five volumes.

That may sound like damning criticism. In fact, the author's numerous bee-infested bonnets are a delight, as is the way his enthusiasms inform, for example, an extended discussion of Debussy or the radically Russophile conception of early 20th-century works. After all, however objective we may aim to be in historical discussion of the arts, the truth is that we are interested in art because we like it.

There are two intellectual bugbears which do wreak some historiographical havoc. Mr Taruskin has a profound distaste for obscurity in all its forms; Schoenberg, in particular, seems to be the object of a personal vendetta. He also deeply mistrusts the system of patronage which has proved such a mixed blessing throughout music's long history.

The intellectual sources for these prejudices are, however, impeccable. Mr Taruskin's feeling about music is that it is neither pure entertainment nor pure formal play. Instead, he makes every effort to show the degree to which music not only reflects life but participates in it. The misleading debate on "progress" is studiously ignored. The result is a refreshingly open-ended view of contemporary music-making that puts many of his predecessors, Burney among them, to shame.

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Benson

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Benson, England's best-loved fish, died on July 29th, aged about 25

SWNS.COM



PETERBOROUGH, in the English Midlands, is a red-brick town, best known as the midway point on the line between King's Cross and York. But from the bottom of Kingfisher Lake, just outside it, urban toil seems far away. There, all is most delightful silt and slime. A push of your probing nose sends up puffs and clouds of fine mud through the water. A riff of bubbles rises, silvery, towards the surface. The green reeds quiver, and sunlight ripples down almost to the depths where you are lurking, plump and still.

Such was mostly the life, and such was the address, of Benson, England's most famous fish. Her actual place of birth, as a wriggling, transparent fry prey to every frog, pike and heron, was never known. But at ten, when she was stocked in Kingfisher, she was already a bruiser. And there, among the willow-shaded banks, she grew. And grew. At her peak weight, in 2006, she was 64lb 2oz (29kg), and was almost circular, like a puffed-up plaice. Bigger carp have been seen in Thailand and in France; but she still amounted to a lot of gefilte fish.

In her glory days she reminded some of Marilyn Monroe, others of Raquel Welch. She was lither than either as she cruised through the water-weed, a lazy twist of gold. Her gleaming scales, said one fan, were as perfect as if they had been painted on. Some wag had named her after a small black hole in her dorsal fin which looked, to him, like a cigarette burn. It was as beautiful and distinctive as a mole on an 18th-century belle. Her lips were full, sultry or sulking, her expression unblinking; she seldom smiled. Yet the reeds held fond memories of her friend Hedges, her companion in slinky swimming until she, or he, was carried away in 1998 by the waters of the River Nene.

Abandoned, she ate more. She devoured everything. Worms, plankton, crayfish, lily roots, disappeared down her toothed, capacious throat. She was a one-fish Hoover, motoring through the food-packed sludge and through rich layers of sedimentary smells. But she was offered daintier and more exotic fare. Cubes of cheese, scraps of luncheon meat, bread crusts, Peperami, dog biscuits and tutti-frutti balls all came down invitingly through the water. She sampled most of them.

Of course, she was not fool enough to think they came from heaven. Carp are cunning, a very fox of the river, as Izaak Walton said. She could see the lines, and at the end of them the trembling shadows of Bert, or Mike, or Stan, spending an idle Sunday away from the wife with a brolly and a can of beer. Often

she continued to lurk, roiling the mud to conceal herself and basking in her own scaled beauty, as carp will. On hot days she would rise to the surface, glowing and tantalising, with a lily-leaf shading her like a parasol. She played hard-to-get, or the One That Got Away, nudging the line before drifting down towards the dark serene. But then, just for the hell of it, she would take the bait.

The first hookings hurt like hell, the whole weight of her body tearing her tongue like a razor blade. But over the years she got used to it, and her leathery mouth would seize the bait as a prize. Hauled to the limelight, she was admirably unphased. This was, after all, the homage beauty was owed. She would submit to the scales and then pose for the photographer, unmoving, holding her breath. She had her picture taken with Tony, owner of her lake, who confessed to the *Wall Street Journal* that he had "quite a rapport" with her; with Ray, who caught her at two in the morning, disturbing her beauty sleep; with Matt, of the shy smile and the woolly hat; with bearded Kyle, for whom she looked especially dark and pouting; and with Steve, who ungallantly told *Peterborough Today* that she felt like "a sack of potatoes" and was "available to everyone". She was not, but at least 50 others held her, or gripped her, for a moment or so. Uncomplainingly, she nestled in their arms before she was lowered to her element again.

These men had a knowledgeable air about them. They might have been a secret society, meeting at odd hours in hidden nooks around the lake. Each had his spot for anoracked meditation. When they spoke, it was of wagglers and clips, spods and backbiters, size 14s and number 8 elastic. Dates and weights were bandied about, an arcane code. For a while, Benson imbibed the philosophy of a gaudier and more complex sphere, heard the tinny music of their radios and stared into the dazzle of the day. There was much that she herself might have imparted, of the mystery of reflected and inverted things. But her anglers needed to get home to the football and their tea.

The fatal nut

Greed probably undid her in the end. She was said to have taken a bait of uncooked tiger nuts, which swelled inside her until she floated upwards. Telltale empty paper bags were found on the bank of the river. Or she may have been pregnant, with 300,000 eggs causing complications, or stressed after so much catching and releasing, those constant brushes with extinction. On the line between life and death, at Kingfisher Lake, she breathed the fatal air and did not sink again. And there she lay, like Wisdom drawn up from the deep: as golden, and as quiet.

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Overview

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Hopes for economic recovery in **America** were raised by July's jobs-market figures. The unemployment rate edged down to 9.4%, from 9.5% in June. American employers, excluding farms, cut 247,000 workers from their payrolls, the smallest monthly jobs loss since August 2008.

The **euro-area economy** may also have reached bottom. GDP in the 16-nation currency zone fell by 0.1% in the three months to the end of June, after a 2.5% drop in the first quarter. France and Germany are already recovering. Germany's GDP rose by 0.3% in the quarter; France's GDP also rose by 0.3%. Most of the region's other economies were still struggling. GDP in the Netherlands sank by 0.9% in the second quarter, Austria's GDP fell by 0.4% and Italy's by 0.5%.

China's economy continued to race ahead. Industrial production rose by 10.8% in the year to July, slightly stronger than the rate in June. The value of retail sales rose by 15.2% from a year earlier; passenger-car sales were up 70.5% from last July. China's rapid recovery has not yet fuelled inflation. Consumer prices fell by 1.8% in the year to July.

Industrial production in **India** rose by 7.8% in the 12 months to June.

The unemployment rate in **Britain** rose from 7.1% to 7.8% in the three months to June. A timelier measure suggests that jobs are being lost at a slower rate. The number claiming unemployment benefit rose by 24,900 in July, compared with an average monthly rise of 93,400 in the first quarter.

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Output, prices and jobs

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Output, prices and jobs

% change on year ago

	Gross domestic product				Industrial production	Consumer prices			Unemployment
	latest	qtr*	2009†	2010†	latest	latest	year ago	2009†	rate‡, %
United States	−3.9 Q2	−1.0	−2.6	+2.0	−13.6 Jun	−1.4 Jun	+5.0	−0.3	9.4 Jul
Japan	−8.8 Q1	−14.2	−6.4	+1.1	−23.5 Jun	−1.8 Jun	+2.0	−1.1	5.4 Jun
China	+7.9 Q2	na	+8.0	+8.0	+10.8 Jul	−1.8 Jul	+6.3	−0.6	9.0 2008
Britain	−5.6 Q2	−3.2	−4.2	+1.0	−11.0 Jun	+1.8 Jun§	+3.8	+1.8	7.8 May††
Canada	−2.1 Q1	−5.4	−2.2	+1.8	−11.8 May	−0.3 Jun	+3.1	+0.5	8.6 Jul
Euro area	−4.6 Q2	−0.4	−4.4	+0.6	−17.0 Jun	−0.6 Jul	+4.0	+0.5	9.4 Jun
Austria	−3.5 Q1	−10.6	−3.2	+0.2	−13.5 May	nil Jun	+3.9	+0.5	4.4 Jun
Belgium	−3.8 Q2	+1.6	−3.5	+0.4	−17.3 May	−1.7 Jul	+5.9	+0.3	11.3 Jun‡‡
France	−2.6 Q2	+1.4	−2.8	+0.8	−12.8 Jun	−0.7 Jul	+3.6	+0.2	9.4 Jun
Germany	−5.9 Q2	+1.3	−5.9	+0.8	−18.0 Jun	−0.5 Jul	+3.3	+0.2	8.3 Jul
Greece	−0.2 Q2	+1.3	−3.1	−0.8	−11.4 Jun	+0.6 Jul	+4.9	+0.5	8.5 May
Italy	−6.0 Q2	−1.9	−5.1	+0.4	−21.9 Jun	nil Jul	+4.1	+0.8	7.3 Q1
Netherlands	−5.1 Q2	−3.4	−4.3	+0.7	−12.7 Jun	+0.2 Jul	+3.2	+1.3	4.7 Jun††
Spain	−3.0 Q1	−7.4	−3.9	−0.6	−14.5 Jun	−1.4 Jul	+5.3	−0.4	18.1 Jun
Czech Republic	−3.4 Q1	−12.9	−3.5	+1.2	−12.2 Jun	+0.3 Jul	+6.9	+1.5	8.4 Jul
Denmark	−4.1 Q1	−4.2	−3.9	+0.6	−18.6 Jun†††	+1.0 Jul	+4.0	+1.1	3.8 Jun
Hungary	−6.7 Q1	−9.6	−6.3	−1.0	−18.6 Jun	+5.1 Jul	+6.7	+4.3	9.6 Jun††
Norway	+1.5 Q1	−1.8	−2.0	+0.5	−6.3 Jun	+2.2 Jul	+4.3	+2.1	3.1 Apr***
Poland	+0.8 Q1	na	−0.8	+1.5	−4.3 Jun	+3.5 Jun	+4.6	+3.2	10.7 Jun‡‡
Russia	−10.9 Q2	na	−7.0	+2.5	−12.1 Jun	+12.0 Jul	+14.7	+12.2	8.3 Jun‡‡
Sweden	−6.2 Q2	−0.1	−4.9	+1.3	−20.8 Jun	−0.9 Jul	+4.1	−0.2	9.8 Jun‡‡
Switzerland	−2.4 Q1	−16.0	−2.3	+0.4	−9.4 Q1	−1.2 Jul	+3.1	−0.5	3.9 Jul
Turkey	−13.8 Q1	na	−5.6	+2.3	−9.7 Jun	+5.4 Jul	+12.1	+6.2	14.9 Apr‡‡
Australia	+0.4 Q1	+1.5	nil	+1.8	−3.6 Q1	+1.5 Q2	+4.5	+1.7	5.8 Jul
Hong Kong	−7.8 Q1	−16.1	−5.4	+2.6	−10.2 Q1	−0.9 Jun	+6.1	nil	5.4 Jun††
India	+5.8 Q1	na	+5.5	+6.3	+7.8 Jun	+9.3 Jun	+7.7	+6.0	6.8 2008
Indonesia	+4.0 Q2	na	+2.6	+3.4	+1.8 May	+2.7 Jul	+11.9	+4.3	8.1 Feb
Malaysia	−6.2 Q1	na	−5.0	+3.3	−9.6 Jun	−1.4 Jun	+7.7	−0.3	4.0 Q1
Pakistan	+2.0 2009**	na	+3.7	+2.8	−11.0 May	+11.2 Jul	+24.3	+12.0	5.2 2008
Singapore	−3.5 Q2	+20.7	−8.6	+1.3	−9.3 Jun	−0.5 Jun	+7.5	−0.2	3.3 Q2
South Korea	−2.5 Q2	+9.7	−4.4	+0.5	−1.2 Jun	+1.6 Jul	+5.9	+2.4	3.8 Jul
Taiwan	−10.2 Q1	na	−6.5	+0.6	−11.4 Jun	−2.3 Jul	+5.8	−1.3	5.9 Jun
Thailand	−7.1 Q1	−7.3	−4.5	+1.9	−7.8 Jun	−4.4 Jul	+9.2	−1.0	2.4 May
Argentina	+2.0 Q1	+0.2	−3.5	+0.7	−2.7 Jun	+5.5 Jul	+9.1	+6.8	8.4 Q1‡‡
Brazil	−1.8 Q1	−3.3	−1.0	+2.7	−10.9 Jun	+4.5 Jul	+6.4	+4.9	8.1 Jun‡‡
Chile	−2.1 Q1	−2.4	−1.0	+2.2	−8.3 Jun	+0.3 Jul	+9.5	+2.1	10.7 Jun††‡‡
Colombia	−0.6 Q1	+0.9	−1.0	+2.5	−6.5 May	+3.3 Jul	+7.5	+4.8	11.4 Jun‡‡
Mexico	−8.2 Q1	−21.5	−7.1	+2.8	−10.6 Jun	+5.4 Jul	+5.4	+5.5	5.2 Jun‡‡
Venezuela	+0.3 Q1	na	−4.2	−2.7	+11.4 Mar	+28.3 Jul	+33.7	+28.0	7.7 Q2‡‡
Egypt	+4.3 Q1	na	+4.4	+4.0	+5.8 Q1	+9.8 Jul	+22.2	+9.7	9.4 Q1‡‡
Israel	+0.6 Q1	−3.6	−1.3	+1.5	−9.8 May	+3.6 Jun	+4.8	+2.8	7.6 Q1
Saudi Arabia	+4.2 2008	na	−1.0	+3.3	na	+5.2 Jun	+10.6	+4.3	na
South Africa	−1.3 Q1	−6.4	−2.2	+3.1	−17.1 Jun	+6.9 Jun	+12.2	+7.1	23.6 Jun‡‡
MORE COUNTRIES Data for the countries below are not provided in printed editions of *The Economist*									
Estonia	−16.6 Q2	na	−13.0	−3.0	−30.1 Jun	−0.7 Jul	+11.1	+0.2	15.6 May
Finland	−7.6 Q1	−10.3	−5.7	−0.1	−20.3 Jun	−0.1 Jun	+4.4	+0.1	8.8 Jun
Iceland	−3.9 Q1	−13.6	−6.5	+0.4	+10.1 2008	+11.3 Jul	+13.6	+12.5	8.1 Jun‡‡
Ireland	−8.5 Q1	−5.7	−7.7	−2.6	+2.6 Jun	−5.4 Jun	+5.0	−3.6	12.2 Jul
Latvia	−18.0 Q1	na	−17.0	−4.0	−18.5 Jun	+2.5 Jul	+16.6	+3.0	16.3 May
Lithuania	−22.4 Q2	−40.8	−15.0	−4.5	−16.3 Jun	+3.0 Jul	+12.2	+5.3	9.3 Jun‡‡
Luxembourg	−5.5 Q1	−5.9	−4.9	−0.8	−25.9 Apr	−0.3 Jun	+4.3	+0.5	5.4 Jun‡‡
New Zealand	−2.2 Q1	−2.7	−2.1	+0.7	−11.4 Q1	+1.9 Q2	+4.0	+1.8	6.0 Q2
Peru	+0.5 May	na	+1.3	+2.7	−8.6 May	+2.7 Jul	+5.8	+3.5	8.3 Jun‡‡
Philippines	+0.4 Q1	−8.9	−1.0	+3.7	−13.0 May	+0.2 Jul	+12.3	+2.9	7.5 Q2‡‡
Portugal	−3.7 Q1	−6.2	−4.1	−0.4	−9.5 Jun	−1.5 Jul	+3.1	−0.7	8.9 Q1‡‡
Slovakia	−5.3 Q2	na	−5.5	+0.7	+19.6 Jun	+2.5 Jul	+4.9	+1.8	11.8 Jun‡‡
Slovenia	−8.5 Q1	na	−6.0	nil	−19.8 May	−0.6 Jul	+6.9	+1.1	8.9 May‡‡
Ukraine	−20.3 Q1	na	−17.0	+1.0	−27.5 Jun	+15.5 Jul	+26.8	+16.0	2.4 Jun
Vietnam	+4.5 Q2	na	+4.2	+4.8	+8.2 Jun	+3.3 Jul	+27.0	+5.6	4.6 2007

*% change on previous quarter, annual rate. †*The Economist* poll or Economist Intelligence Unit estimate/forecast. ‡National definitions. §RPI inflation rate -1.6 in June. **Year ending June. ††Latest three months. ‡‡Not seasonally adjusted. ***Centred 3-month average

Sources: National statistics offices and central banks; Thomson Datastream; Reuters; Centre for Monitoring Indian Economy; OECD; ECB

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The Economist commodity-price index

Aug 13th 2009
From The Economist print edition

The Economist commodity-price index
2000=100

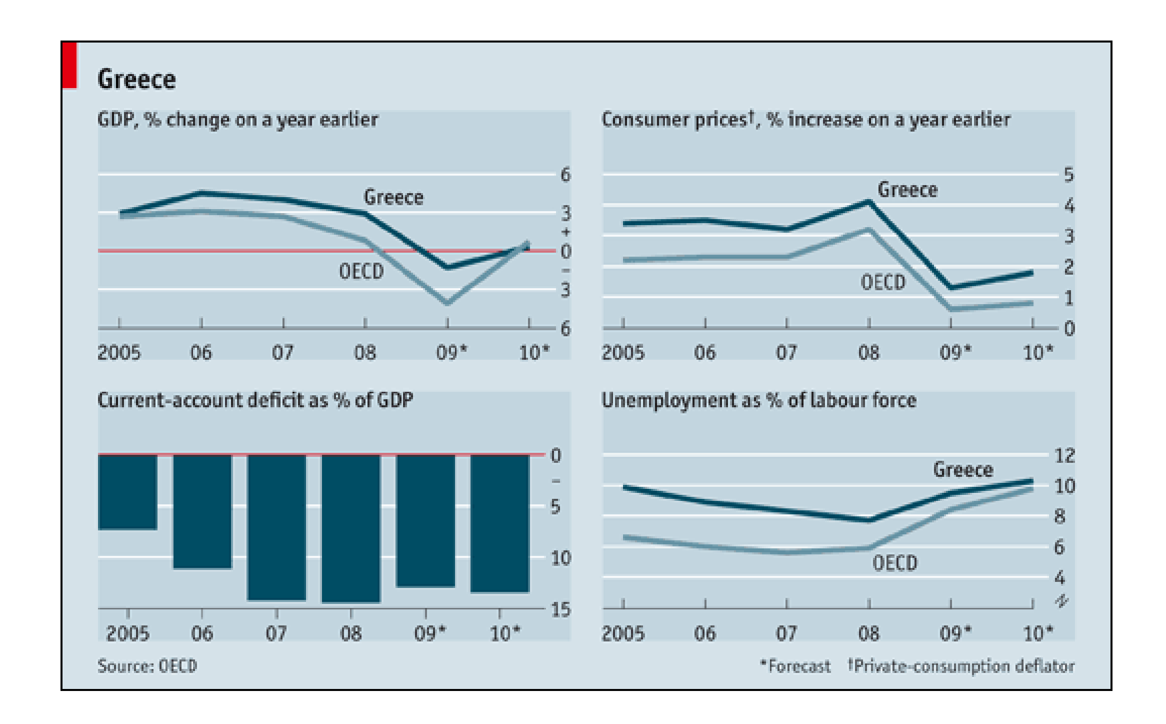
	Aug 4th	Aug 11th*	% change on one month	% change on one year
Dollar index				
All items	196.0	198.6	+11.4	-15.3
Food	207.8	207.5	+5.7	-13.0
Industrials				
All	180.9	187.0	+20.7	-18.3
Nfa†	141.0	146.5	+14.0	-22.9
Metals	202.6	209.2	+23.5	-16.4
Sterling index				
All items	175.8	182.5	+9.9	-2.4
Euro index				
All items	125.9	129.9	+9.9	-10.7
Gold				
$ per oz	964.00	943.75	+2.5	+15.8
West Texas Intermediate				
$ per barrel	71.33	69.38	+16.6	-38.8

*Provisional †Non-food agriculturals.

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Greece

Aug 13th 2009
From The Economist print edition



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Trade, exchange rates, budget balances and interest rates

Aug 13th 2009
From The Economist print edition

Trade, exchange rates, budget balances and interest rates

	Trade balance* latest 12 months, $bn	Current-account balance latest 12 months, $bn	Current-account balance % of GDP 2009†	Currency units, per $ Aug 12th	Currency units, per $ year ago	Budget balance % of GDP 2009†	Interest rates, % 3-month latest	Interest rates, % 10-year gov't bonds, latest
United States	−639.5 Jun	−628.3 Q1	−3.0	–	–	−13.7	0.21	3.70
Japan	+9.0 Jun	+115.3 Jun	+2.5	96.2	109	−7.9	0.40	1.42
China	+269.4 Jul	+426.1 Q4	+6.5	6.84	6.86	−4.1	1.73	3.74
Britain	−139.8 Jun	−52.5 Q1	−1.7	0.60	0.54	−14.4	0.90	3.93
Canada	+15.5 Jun	−3.9 Q1	−2.3	1.09	1.07	−2.3	0.24	3.51
Euro area	−46.2 May	−158.1 May	−1.3	0.70	0.67	−5.9	0.88	3.48
Austria	−5.5 May	+10.7 Q1	+1.6	0.70	0.67	−5.2	0.88	3.83
Belgium	+6.0 Apr	−12.0 Mar	−2.4	0.70	0.67	−6.0	0.90	3.84
France	−71.1 Jun	−58.3 Jun	−2.1	0.70	0.67	−8.2	0.88	3.61
Germany	+182.0 Jun	+171.0 May	+3.7	0.70	0.67	−4.7	0.88	3.45
Greece	−56.2 Apr	−42.9 May	−9.0	0.70	0.67	−6.1	0.88	4.57
Italy	−11.9 May	−63.1 May	−2.8	0.70	0.67	−5.2	0.88	4.18
Netherlands	+44.1 May	+50.0 Q1	+6.1	0.70	0.67	−4.2	0.88	3.69
Spain	−101.4 May	−117.2 May	−7.1	0.70	0.67	−10.3	0.88	3.89
Czech Republic	+4.3 Jun	−4.7 Jun	−2.0	18.2	16.2	−4.8	1.89	5.16
Denmark	+6.2 Jun	+8.1 Jun	+1.5	5.24	5.02	−2.5	1.98	3.70
Hungary	+2.0 Jun	−11.3 Q1	−2.9	191	160	−3.9	8.45	8.80
Norway	+61.0 Jun	+79.6 Q1	+14.4	6.11	5.39	7.4	1.79	4.24
Poland	−16.2 May	−11.7 Jun	−3.3	2.92	2.22	−3.9	4.15	6.11
Russia	+122.2 Jun	+55.3 Q2	+1.9	32.4	24.3	−8.0	10.75	11.26
Sweden	+13.6 Jun	+31.4 Q1	+6.7	7.19	6.30	−4.7	0.13	3.49
Switzerland	+16.9 Jun	+56.6 Q1	+7.4	1.08	1.09	−3.1	0.35	1.99
Turkey	−47.4 Apr	−23.8 May	−0.4	1.49	1.19	−5.8	8.70	6.12‡
Australia	+5.7 Jun	−29.8 Q1	−4.0	1.20	1.15	−4.0	3.30	5.57
Hong Kong	−20.7 Jun	+29.3 Q1	+9.2	7.75	7.81	−3.9	0.23	2.49
India	−93.4 Jun	−29.8 Q1	−1.2	48.4	42.6	−7.8	3.27	7.60
Indonesia	+11.2 Jun	−0.8 Q1	+0.7	9,955	9,180	−3.0	7.05	6.60‡
Malaysia	+38.2 Jun	+40.5 Q1	+14.1	3.53	3.32	−8.0	2.14	2.27‡
Pakistan	−16.3 Jul	−12.2 Q1	−2.1	82.7	75.3	−4.3	12.19	12.52‡
Singapore	+17.4 Jun	+23.1 Q1	+15.4	1.44	1.40	−4.1	0.50	2.33
South Korea	+21.9 Jul	+20.7 Jun	+2.7	1,246	1,039	−5.4	2.41	5.33
Taiwan	+15.9 Jul	+29.2 Q1	+10.4	32.9	31.1	−5.2	0.85	1.37
Thailand	+10.2 Jun	+8.1 Jun	+5.3	34.0	33.6	−5.6	1.38	3.21
Argentina	+17.1 Jun	+6.8 Q1	+2.6	3.83	3.04	−1.3	14.38	na
Brazil	+27.1 Jul	−18.4 Jun	−1.3	1.83	1.63	−2.8	8.65	6.16‡
Chile	+4.5 Jul	−4.3 Q1	−0.9	546	518	−4.1	0.48	2.60‡
Colombia	−0.1 Jun	−6.5 Q1	−3.3	2,024	1,857	−3.0	5.04	5.79‡
Mexico	−16.0 Jun	−14.2 Q1	−2.7	13.0	10.2	−4.0	4.49	8.03
Venezuela	+32.5 Q1	+26.2 Q1	+1.4	6.69	3.33§	−7.6	14.53	6.55‡
Egypt	−26.1 Q1	−2.9 Q1	−1.8	5.55	5.33	−6.8	9.89	2.94‡
Israel	−8.7 Jul	+4.1 Q1	+2.2	3.83	3.60	−6.1	0.56	4.22
Saudi Arabia	+197.4 2008	+124.0 2008	+4.5	3.75	3.75	−0.5	0.65	na
South Africa	−5.4 Jun	−18.7 Q1	−5.8	8.08	7.90	−4.5	7.75	9.02
MORE COUNTRIES Data for the countries below are not provided in printed editions of *The Economist*								
Estonia	−2.2 Jun	−0.8 May	+0.7	11.0	10.5	−3.7	6.08	na
Finland	+6.3 May	+4.2 May	+1.0	0.70	0.67	−2.6	0.81	3.72
Iceland	+0.7 Jul	−6.1 Q1	−5.9	127	82.4	−13.3	7.72	na
Ireland	+47.7 May	−11.3 Q1	−3.1	0.70	0.67	−12.9	0.88	4.84
Latvia	−4.3 May	−1.7 May	−2.0	0.49	0.47	−11.0	11.99	na
Lithuania	−4.3 May	−2.2 May	−0.3	2.43	2.32	−6.9	7.99	na
Luxembourg	−7.3 Apr	+2.2 Q1	na	0.70	0.67	−4.0	0.88	na
New Zealand	−2.3 Jun	−11.8 Q1	−7.1	1.49	1.44	−6.7	3.70	5.90
Peru	+2.3 Jun	−3.8 Q1	−2.3	2.93	2.95	−2.3	1.25	na
Philippines	−6.9 May	+5.1 Mar	+4.5	48.1	44.7	−3.1	4.25	na
Portugal	−28.2 Jun	−24.5 May	−8.7	0.70	0.67	−7.0	0.88	4.04
Slovakia	−0.3 May	−5.4 May	−7.0	21.2	20.4	−5.5	1.35	4.33
Slovenia	−3.4 May	−2.1 Apr	−1.6	0.70	0.67	−5.7	0.88	na
Ukraine	−13.4 Q1	−6.5 Q2	−0.4	8.23	4.62	−7.0	12.01	na
Vietnam	−5.4 Jul	−7.0 2007	−6.9	17,811	16,625	−9.0	8.43	6.30

*Merchandise trade only. †The Economist poll or Economist Intelligence Unit forecast. ‡Dollar-denominated bonds. §Unofficial exchange rate.

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Markets

Aug 13th 2009
From The Economist print edition

Markets

	Index Aug 12th	% change on one week	% change on Dec 31st 2008 in local currency	% change on Dec 31st 2008 in $ terms
United States (DJIA)	9,361.6	+0.9	+6.7	+6.7
United States (S&P 500)	1,005.8	+0.3	+11.4	+11.4
United States (NAScomp)	1,998.7	+0.3	+26.7	+26.7
Japan (Nikkei 225)	10,435.0	+1.8	+17.8	+11.0
Japan (Topix)	959.9	+1.1	+11.7	+5.2
China (SSEA)	3,267.0	−9.2	+70.9	+70.6
China (SSEB, $ terms)	209.3	−5.6	+89.1	+88.7
Britain (FTSE 100)	4,716.8	+1.5	+6.4	+22.3
Canada (S&P TSX)	10,659.9	−3.5	+18.6	+34.5
Euro area (FTSE Euro 100)	826.7	+1.4	+10.8	+13.3
Euro area (DJ STOXX 50)	2,688.2	+1.7	+9.8	+12.3
Austria (ATX)	2,326.7	−0.5	+32.9	+35.9
Belgium (Bel 20)	2,273.3	+4.6	+19.1	+21.8
France (CAC 40)	3,507.2	+1.4	+9.0	+11.4
Germany (DAX)*	5,350.1	−0.1	+11.2	+13.7
Greece (Athex Comp)	2,295.7	−4.0	+28.5	+31.4
Italy (S&P/MIB)	21,546.4	+2.8	+10.7	+13.2
Netherlands (AEX)	289.0	+1.3	+17.5	+20.1
Spain (Madrid SE)	1,139.9	+2.3	+16.8	+19.4
Czech Republic (PX)	1,114.9	−0.5	+29.9	+38.1
Denmark (OMXCB)	303.0	+0.4	+33.9	+36.9
Hungary (BUX)	18,071.8	+2.7	+47.6	+47.7
Norway (OSEAX)	350.8	−0.4	+29.8	+48.7
Poland (WIG)	35,224.8	+1.6	+29.4	+31.1
Russia (RTS, $ terms)	1,025.1	−6.3	+72.1	+62.2
Sweden (OMXS30)†	876.7	+0.3	+32.4	+45.5
Switzerland (SMI)	5,962.5	+0.9	+7.7	+6.5
Turkey (ISE)	43,889.8	nil	+63.4	+68.8
Australia (All Ord.)	4,345.9	+1.7	+18.8	+40.2
Hong Kong (Hang Seng)	20,435.2	−0.3	+42.0	+42.0
India (BSE)	15,020.2	−5.6	+55.7	+56.8
Indonesia (JSX)	2,347.4	+1.3	+73.2	+89.6
Malaysia (KLSE)	1,180.5	+0.1	+34.6	+32.0
Pakistan (KSE)	8,058.5	+2.9	+37.4	+31.5
Singapore (STI)	2,571.3	−1.4	+46.0	+45.7
South Korea (KOSPI)	1,565.4	+0.4	+39.2	+40.7
Taiwan (TWI)	6,898.9	+0.7	+50.3	+49.7
Thailand (SET)	643.0	+0.4	+42.9	+46.0
Argentina (MERV)	1,773.3	−1.8	+64.2	+48.0
Brazil (BVSP)	56,588.0	+0.4	+50.7	+91.6
Chile (IGPA)	15,459.1	−0.9	+36.5	+59.3
Colombia (IGBC)	10,426.1	+0.5	+37.9	+53.2
Mexico (IPC)	28,096.0	nil	+25.5	+33.7
Venezuela (IBC)	48,275.3	+4.1	+37.6	+48.1
Egypt (Case 30)	6,283.4	−2.8	+36.7	+35.8
Israel (TA-100)	879.4	−3.4	+55.9	+53.7
Saudi Arabia (Tadawul)	5,845.7	+1.3	+21.7	+21.8
South Africa (JSE AS)	24,588.5	−1.3	+14.3	+30.8
Europe (FTSEurofirst 300)	942.1	+0.8	+13.2	+15.8
World, dev'd (MSCI)	1,058.6	−0.3	+15.0	+15.0
Emerging markets (MSCI)	840.2	−1.7	+48.2	+48.2
World, all (MSCI)	269.1	−0.5	+18.2	+18.2
World bonds (Citigroup)	807.4	−1.0	−0.3	−0.3
EMBI+ (JPMorgan)	457.4	−0.8	+16.8	+16.8
Hedge funds (HFRX)§	1,101.5	nil	+7.9	+7.9
Volatility, US (VIX)	25.5	24.9	40.0	(levels)
CDSs, Eur (iTRAXX)‡	110.4	+4.9	−45.4	−44.1
CDSs, N Am (CDX)‡	176.5	+13.6	−24.4	−24.4
Carbon trading (EU ETS) €	14.4	−0.2	−10.9	−8.9

*Total return index. †New series. ‡Credit-default swap spreads, basis points.
Sources: National statistics offices, central banks and stock exchanges; Thomson Reuters; WM/Reuters; JPMorgan Chase; Bank Leumi le-Israel; CBOE; CMIE; Danske Bank; EEX; HKMA; Markit; Standard Bank Group; UBS; Westpac. §Aug 11th

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Office vacancy rates

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The global recession has led to an increase in empty office space in most big cities across the world, according to CB Richard Ellis, a property firm. Beijing's office glut was already the worst of any large city a year ago. But it has since worsened and the vacancy rate is now 23%. Thanks to the severe downturn in the Russian economy, the fraction of offices lying unoccupied has more than doubled in Moscow. About one-eighth of office space is vacant in both Mumbai and Frankfurt. But Frankfurt's vacancy rate has hardly budged over the past year, whereas Mumbai's has more than quadrupled, from 2.9% to 12.7%. Occupancy has fallen even in crowded Tokyo, but its vacancy rate of 5.1% is still the lowest of any big city.

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